

The Fraud in the Inducement Exception to the Economic Loss Doctrine

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THE FRAUD IN THE INDUCEMENT EXCEPTION TO THE ECONOMIC LOSS DOCTRINE

RALPH C. ANZIVINO*

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I. INTRODUCTION

The dividing line between contract and tort law has always been a difficult one to draw. The sale of a product generally involves two broad concerns. One concern is a private one that contracting parties can agree on the terms of a private sale within defined limits. The second concern is a public concern that the product sold not cause any injury or damage. The economic loss doctrine follows this public/private line of demarcation. The doctrine draws the line between contract and tort based on the type of damages suffered when the product does not meet contract specifications. The economic loss doctrine concludes that if a defective product causes solely economic loss, the dispute is essentially a private matter between the contracting parties and their contract should control their dispute. The public interest is not sufficiently involved to merit tort involvement. On the other hand, if a defective product causes personal injury or other property damage, then the public interest is involved and a tort approach, free of contractual limitations, is most apt. The doctrine has merit.

Difficulties arise, however, when one is fraudulently induced to enter into a contract for a product, and only economic loss is incurred. There is no personal injury or other property damage. How does the fraud impact where the line is drawn under the economic loss doctrine? Is the public interest sufficiently involved to invoke tort law, or is this still a private matter between private contracting parties that invokes only contract law? The states have taken a number of different positions on this issue. Most states have adopted the broad fraud in the inducement exception to the economic loss doctrine. The broad exception provides that the fraud is an intentional tort, and as such, the intentional misrepresentation is actionable as a tort, notwithstanding that the contract losses are solely economic. A small minority of states, including recently Wisconsin, has adopted the narrow fraud in the inducement exception to the economic loss doctrine. The narrow exception provides that if the fraudulent inducement relates to interwoven fraud, then the fraud is not actionable under tort law, only

contract law. The only fraud actionable under the narrow fraud in the inducement exception is fraud considered to be extraneous to the contract. The purpose of this Article is to examine the narrow fraud in the inducement exception to the economic loss doctrine under Wisconsin case law, statutes, and public policy to determine if it is a sound principle.

II. THE DIFFERENCES BETWEEN CONTRACT AND TORT ACTIONS

Because the economic loss doctrine determines whether a matter proceeds in court as a tort or contract action, that decision is a significant one. There are many differences between a tort and contract action. First, privity is generally required in a contract action but not in tort.¹ Second, the statutes of limitations are different.² The contract statute of limitations is generally six years,³ and the statute of limitations for tort can be two⁴ or three years.⁵ Third, there are different pleading requirements for a fraud case⁶ as compared to a contract case.⁷ Fourth, the burdens of proof are different. The burden of proof in a contract case is by “preponderance of the evidence,”⁸ and for a fraud case, it is “clear and convincing evidence.”⁹ Fifth, tort damages are designed to return the aggrieved party to his or her pre-event condition and also serve as a vehicle to deter similar conduct from the tortfeasor and others in the future.¹⁰ Contract damages are typically expectancy damages to place the aggrieved party in the position he or she would have been in had the contract been performed.¹¹ Sixth, punitive damages are available for intentional tortious conduct¹² but

1. *Northridge Co. v. W.R. Grace & Co.*, 162 Wis. 2d 918, 932–33, 471 N.W.2d 179, 184 (1991); *Grams v. Milk Prods., Inc.*, 2005 WI 112, ¶¶ 69–70, 283 Wis. 2d 511, ¶¶ 69–70, 699 N.W.2d 167, ¶¶ 69–70.

2. *Northridge Co.*, 162 Wis. 2d at 932–33, 471 N.W.2d at 184; *Grams*, 2005 WI 112, ¶¶ 69–70, 283 Wis. 2d 511, ¶¶ 69–70, 699 N.W.2d 167, ¶¶ 69–70.

3. WIS. STAT. § 893.43 (2005–2006) (action on contract).

4. *Id.* § 893.57 (intentional torts).

5. *Id.* § 893.54 (injury to the person).

6. *Id.* § 802.03(2) (pleading special matters—fraud, mistake, and condition of mind); *All-Tech Telecom, Inc. v. Amway Corp.*, 174 F.3d 862, 867 (7th Cir. 1999).

7. WIS. STAT. § 425.109(1)(h); *All-Tech*, 174 F.3d at 867.

8. *Carle v. Nelson*, 145 Wis. 593, 598, 130 N.W. 467, 469 (1911).

9. *Digicorp, Inc. v. Ameritech Corp.*, 2003 WI 54, ¶ 52, 262 Wis. 2d 32, ¶ 52, 662 N.W.2d 652, ¶ 52; *see also* *Lundin v. Shimanski*, 124 Wis. 2d 175, 184, 368 N.W.2d 676, 681 (1985).

10. *Jeffers v. Nysse*, 98 Wis. 2d 543, 547–48, 297 N.W.2d 495, 497 (1980).

11. RESTATEMENT (SECOND) OF CONTRACTS § 344 cmt. a (1981).

12. *See Strenke v. Hogner*, 2005 WI 25, ¶ 38, 279 Wis. 2d 52, ¶ 38, 694 N.W.2d 296, ¶ 38.

rarely are available in a contract action.¹³ Tort law offers a broader array of damages than contract law.¹⁴ Any of the foregoing differences may be critical depending upon the specifics of each case. When the economic loss doctrine applies, however, the doctrine mandates that the action be brought in contract, not tort. A forced election of remedy occurs as a result of the economic loss doctrine being applied to a case.

III. THE ECONOMIC LOSS DOCTRINE

The boundary between contract and tort has fluctuated with societal development.¹⁵ Contract and tort law generally serve different interests.¹⁶ Tort duties are imposed by law, and contract duties are imposed by bargaining.¹⁷ Tort duties are imposed to protect society.¹⁸ There is a strong public policy component in tort duties to deter harmful conduct.¹⁹ For example, an intentional misrepresentation is a serious wrong and a serious violation of community mores, which normally invokes tort liability.²⁰ As a general rule, the United States Supreme Court has noted that in cases of overlap between tort and contract liability, tort liability should not be supplanted without good reason.²¹

The majority of jurisdictions in the United States has accepted and endorsed some form of the economic loss doctrine.²² Only a few states have rejected it.²³

13. *White v. Benkowski*, 37 Wis. 2d 285, 290–91, 155 N.W.2d 74, 77 (1967); *Sassara v. Braun*, No. 95-3300, 1997 WL 164020, at *5 (Wis. Ct. App. Apr. 9, 1997).

14. *Grams v. Milk Prods., Inc.*, 2005 WI 112, ¶ 14, 283 Wis. 2d 511, ¶ 14, 699 N.W.2d 167, ¶ 14; *Ins. Co. of N. Am. v. Cease Elec. Inc.*, 2004 WI 139, ¶ 24, 276 Wis. 2d 361, ¶ 24, 688 N.W.2d 462, ¶ 24.

15. *State Farm Mut. Auto. Ins. Co. v. Ford Motor Co.*, 225 Wis. 2d 305, 318, 592 N.W.2d 201, 206 (1999).

16. *Cease*, 2004 WI 139, ¶ 39, 276 Wis. 2d 361, ¶ 39, 688 N.W.2d 462, ¶ 39; *Daanen & Janssen, Inc. v. Cedarapids, Inc.*, 216 Wis. 2d 395, 404–05, 573 N.W.2d 842, 846–77 (1998).

17. *Northridge Co. v. W.R. Grace & Co.*, 162 Wis. 2d 918, 933, 471 N.W.2d 179, 185 (1991).

18. *Daanen & Janssen*, 216 Wis. 2d at 405, 573 N.W.2d at 846.

19. *Cease*, 2004 WI 139, ¶ 41, 276 Wis. 2d 361, ¶ 41, 688 N.W.2d 462, ¶ 41.

20. *See Van Lare v. Vogt, Inc.*, 2004 WI 110, ¶ 26, 274 Wis. 2d 631, ¶ 26, 683 N.W.2d 46, ¶ 26.

21. *Saratoga Fishing Co. v. J.M. Martinac & Co.*, 520 U.S. 875, 882–83 (1997).

22. ALABAMA: *Lloyd Wood Coal Co. v. Clark Equip. Co.*, 543 So. 2d 671, 672–74 (Ala. 1989). ALASKA: *Pratt & Whitney Can., Inc. v. Sheehan*, 852 P.2d 1173, 1177 (Alaska 1993); *St. Denis v. Dep't of Hous. & Urban Dev.*, 900 F. Supp. 1194, 1200 (D. Alaska 1995). ARIZONA: *Salt River Project Agric. Improvement & Power Dist. v. Westinghouse Elec. Corp.*, 694 P.2d 198, 209 (Ariz. 1984); *Carstens v. City of Phoenix*, 75 P.3d 1081, 1084 (Ariz. Ct. App. 2003); *Apollo Group, Inc. v. Avnet, Inc.*, 58 F.3d 477, 479–80 (9th Cir. 1995). CALIFORNIA: *Robinson Helicopter Co. v. Dana Corp.*, 102 P.3d 268, 272–74 (Cal. 2004).

COLORADO: *A.C. Excavating v. Yacht Club II Homeowners Ass'n*, 114 P.3d 862, 865 (Colo. 2005); *Town of Alma v. Azco Constr., Inc.*, 10 P.3d 1256, 1264 (Colo. 2000). CONNECTICUT: CONN. GEN. STAT. § 52-572c(n) (2005); *Flagg Energy Dev. Corp. v. Gen. Motors Corp.*, 709 A.2d 1075, 1088 (Conn. 1998) (applying principles of the economic loss doctrine in a products liability case). *But see Paliwoda v. Mathews*, No. CV020398249S, 2006 Conn. Super. LEXIS 3088, at *16 (Conn. Super. Ct. Oct. 16, 2006) (noting the split in authority in lower courts with regard to meaning of *Flagg*). DELAWARE: *Danforth v. Acorn Structures, Inc.*, 608 A.2d 1194, 1198 (Del. 1992). FLORIDA: *Indem. Ins. Co. of N. Am. v. Am. Aviation, Inc.*, 891 So. 2d 532, 536 (Fla. 2004). GEORGIA: *Gen. Elec. Co. v. Lowe's Home Ctrs., Inc.*, 608 S.E.2d 636, 638 (Ga. 2005). HAWAII: *City Express, Inc. v. Express Partners*, 959 P.2d 836, 839 (Haw. 1998); *State v. U.S. Steel Corp.*, 919 P.2d 294, 302 (Haw. 1996). IDAHO: *Blaht v. Richard B. Smith, Inc.*, 108 P.3d 996, 1000 (Idaho 2005). ILLINOIS: *First Midwest Bank, N.A. v. Stewart Title Guar. Co.*, 843 N.E.2d 327, 333-34 (Ill. 2006); *Moorman Mfg. Co. v. Nat'l Tank Co.*, 435 N.E.2d 443, 450 (Ill. 1982). INDIANA: *Gunkel v. Renovations, Inc.*, 822 N.E.2d 150, 152 (Ind. 2005). IOWA: *Determan v. Johnson*, 613 N.W.2d 259, 261-62 (Iowa 2000). KANSAS: *Prendiville v. Contemporary Homes, Inc.*, 83 P.3d 1257, 1260 (Kan. Ct. App. 2004); *Full Faith Church of Love W., Inc. v. Hoover Treated Wood Prods., Inc.*, 224 F. Supp. 2d 1285, 1289 (D. Kan. 2002) (predicting the Kansas Supreme Court would agree with the Kansas Court of Appeals and endorse the economic loss doctrine). KENTUCKY: *Presnell Constr. Managers, Inc. v. EH Constr., LLC*, 134 S.W.3d 575, 583 (Ky. 2004) (Keller, J., concurring) (stating that the court should explicitly adopt the economic loss doctrine); *Mt. Lebanon Pers. Care Home, Inc. v. Hoover Universal, Inc.*, 276 F.3d 845, 849 (6th Cir. 2002) (predicting the Kentucky Supreme Court would apply the economic loss doctrine to a business purchase). MAINE: *Oceanside at Pine Point Condo. Owners Ass'n v. Peachtree Doors, Inc.*, 659 A.2d 267, 270 (Me. 1995). MARYLAND: *Morris v. Osmose Wood Preserving*, 667 A.2d 624, 631 (Md. 1995). MASSACHUSETTS: *Berish v. Bornstein*, 770 N.E.2d 961, 975 (Mass. 2002). MICHIGAN: *Neibarger v. Universal Coops., Inc.*, 486 N.W.2d 612, 615 (Mich. 1992). MINNESOTA: MINN. STAT. § 604.10 (2006). MISSISSIPPI: *Progressive Ins. Co. v. Monaco Coach Corp.*, No. 1:05cv37-DMR-JMR, 2006 U.S. Dist. LEXIS 21251, at *5 (S.D. Miss. Mar. 29, 2006); *E. Miss. Elec. Power Ass'n v. Porcelain Prods. Co.*, 729 F. Supp. 512, 514 (S.D. Miss. 1990) (predicting that the Mississippi Supreme Court would not allow recovery of solely economic losses stemming from a defective product in tort); *State Farm Mut. Auto. Ins. Co. v. Ford Motor Co.*, 736 So. 2d 384, 387 (Miss. Ct. App. 1999). MISSOURI: *Sharp Bros. Contracting Co. v. Am. Hoist & Derrick Co.*, 703 S.W.2d 901, 903 (Mo. 1986); *Self v. Equilon Enters., LLC*, No. 4:00CV1903 TIA, 2005 U.S. Dist. LEXIS 17288, at *40 (E.D. Mo. Mar. 30, 2005). NEBRASKA: *Nat'l Crane Corp. v. Ohio Steel Tube Co.*, 332 N.W.2d 39, 43 (Neb. 1983). NEVADA: *Calloway v. City of Reno*, 993 P.2d 1259, 1266 (Nev. 2000), *rev'd on other grounds*, *Olson v. Richard*, 89 P.3d 31, 33 (2004). NEW HAMPSHIRE: *Kelleher v. Marvin Lumber & Cedar Co.*, 891 A.2d 477, 495 (N.H. 2005). NEW JERSEY: *Alloway v. Gen. Marine Indus., L.P.*, 695 A.2d 264, 275 (N.J. 1997). NEW MEXICO: *In re Consol. Vista Hills Retaining Wall Litig.*, 893 P.2d 438, 445-46 (N.M. 1995). NEW YORK: *Bocre Leasing Corp. v. Gen. Motors Corp.*, 645 N.E.2d 1195, 1196, 1199 (N.Y. 1995). NORTH CAROLINA: *Moore v. Coachmen Indus., Inc.*, 499 S.E.2d 772, 780 (N.C. Ct. App. 1998). NORTH DAKOTA: *Steiner v. Ford Motor Co.*, 606 N.W.2d 881, 885 (N.D. 2000). OHIO: *Corporex Dev. & Constr. Mgmt., Inc. v. Shook, Inc.*, 835 N.E.2d 701, 704 (Ohio 2005). OKLAHOMA: *Dutsch v. Sea Ray Boats, Inc.*, 845 P.2d 187, 193 (Okla. 1992); *Waggoner v. Town & Country Mobile Homes, Inc.*, 808 P.2d 649, 653 (Okla. 1990); *United Golf, LLC v. Westlake Chem. Corp.*, No. 05-CV-0495-CVE-PJC, 2006 U.S. Dist. LEXIS 57531, at *7 (N.D. Okla. Aug. 15, 2006). OREGON: *Harris v. Suniga*, 149 P.3d 224, 227 (Or. 2006); *Or. Steel Mills, Inc. v. Coopers & Lybrand, LLP*, 83 P.3d 322, 328 (Or. 2004); *Onita Pac. Corp. v. Tr. of Bronson*, 843 P.2d 890, 896-97 (Or. 1992); *Hale v. Groce*, 744 P.2d 1289, 1290 (Or. 1987). PENNSYLVANIA: *Bilt-Rite Contractors v.*

The economic loss doctrine developed largely in response to the extension of product liability law into contract law. Product liability law protects buyers of products from personal injury and damage to other property.²⁴ Product liability law does not cover cases where the loss is solely economic. The theory behind the economic loss doctrine is that once a bargain is struck and contract terms are agreed upon, the buyer should not be able to circumvent the contract terms via tort.²⁵ However, there needs to be a balance struck between honoring the parties' contract and protecting the public from dangerous products.²⁶ Clearly, when one suffers personal injury or other property damage from a defective product, the balance is in favor of tort. On the other hand, when solely economic loss is involved, the balance is in favor of the contract to control the parties' dispute.

The policy arguments for imposing tort duties are diminished where only economic loss is involved.²⁷ "Whether a product meets a certain level of performance or a purchaser's expectations is not a matter of

Architectural Studio, 866 A.2d 270, 286–87 (Pa. 2005). RHODE ISLAND: *Rousseau v. K.N. Constr., Inc.*, 727 A.2d 190, 193 (R.I. 1999) (holding economic loss rule is inapplicable to consumer transactions); *Boston Inv. Prop. #1 State v. E.W. Burman, Inc.*, 658 A.2d 515, 518 (R.I. 1995). SOUTH CAROLINA: *Tommy L. Griffin Plumbing & Heating Co. v. Jordon, Jones & Goulding, Inc.* 463 S.E.2d 85, 88 (S.C. 1995). SOUTH DAKOTA: *Diamond Surface Inc. v. State Cement Plant Comm'n*, 583 N.W.2d 155, 161 (S.D. 1998). TENNESSEE: *Messer Griesheim Indus. Inc. v. Eastman Chem. Co.*, 194 S.W.3d 466, 471–72 (Tenn. Ct. App. 2005); *Trinity Indus. Inc. v. McKinnon Bridge Co.*, 77 S.W.3d 159, 173 (Tenn. Ct. App. 2001). TEXAS: *Formosa Plastics Corp. USA v. Presidio Eng'rs & Contractors*, 960 S.W.2d 41, 45 (Tex. 1998). UTAH: *Hermansen v. Tasulis*, 48 P.3d 235, 240 (Utah 2002). VERMONT: *Hamill v. Pawtucket Mut. Ins. Co.*, 892 A.2d 226, 229 (Vt. 2005). VIRGINIA: *Filak v. George*, 594 S.E.2d 610, 613 (Va. 2004). WASHINGTON: *Alejandro v. Bull*, 98 P.3d 844, 852 (Wash. Ct. App. 2004); *Berschauer/Phillips Constr. Co. v. Seattle Sch. Dist. No. 1*, 881 P.2d 986, 990 (Wash. 1994); *Reynolds Metals Co. v. Alcan Inc.*, No. C04-0175RJB, 2006 U.S. Dist. LEXIS 29033, at *8–*9 (W.D. Wash. Apr. 28, 2006). WEST VIRGINIA: *Aikens v. Debow*, 541 S.E.2d 576, 589 (W. Va. 2000). WISCONSIN: 1325 N. Van Buren, LLC v. T-3 Group, Ltd., 2006 WI 94, ¶ 5, 293 Wis. 2d 410, ¶ 5, 716 N.W.2d 822, ¶ 5. WYOMING: *D & D Transp., Ltd. v. Interline Energy Servs., Inc.*, 117 P.3d 423, 427 (Wyo. 2005).

23. The Supreme Court of Arkansas has chosen not to adopt the economic loss doctrine. *Farm Bureau Ins. Co. v. Case Corp.*, 878 S.W.2d 741, 743 (Ark. 1994); *Blagg v. Fred Hunt Co.*, 612 S.W.2d 321, 324 (Ark. 1981). Montana has likewise declined to follow the economic loss doctrine. *Jim's Excavating Serv., Inc. v. HKM Assocs.*, 878 P.2d 248, 252, 255 (Mont. 1994).

24. RESTATEMENT (THIRD) OF TORTS: PRODUCTS LIABILITY § 21 (1998).

25. *State Farm Mut. Auto. Ins. Co. v. Ford Motor Co.*, 225 Wis. 2d 305, 329–30, 592 N.W.2d 201, 211 (1999).

26. *Stoughton Trailers, Inc. v. Henkel Corp.*, 965 F. Supp. 1227, 1231 (W.D. Wis. 1997).

27. *Daanen & Janssen, Inc. v. Cedarapids, Inc.*, 216 Wis. 2d 395, 405, 573 N.W.2d 842, 847 (1998).

societal interest.”²⁸ Rather it is the domain of contract law.²⁹ Thus, as a general rule, in the absence of any tort concern, contract law is better suited to govern the parties’ dispute. Societal interests direct that the nature of the damages incurred is apparently the tipping point for the economic loss doctrine. A dangerous or defective product that causes no personal injury or other property damage is not actionable under tort law, only contract law.³⁰ Since only economic losses have been incurred, the parties’ contract understandably should govern their dispute. Interject negligence into the transaction, and the economic loss doctrine still provides that the parties’ contract shall control their dispute over the economic losses.³¹ The negligence does not arouse sufficient public policy concerns to permit the aggrieved party to assert the tort to recover solely economic losses. In other words, there is not a sufficient basis to circumvent the contract with a tort claim.

The decision to prefer the contract over negligence is consistent with established contract and tort principles. Under contract law, parties are permitted by contract to exculpate themselves from liability for negligence.³²

Public policy does not disfavor such bargaining. In fact, the economic loss doctrine expects parties to bargain with reference to all foreseeable matters within their contractual relationship.³³ Thus, when the economic loss doctrine mandates that the contract shall govern the recovery of solely economic losses despite negligence, no established public policy is disturbed. In fact, the economic loss doctrine is consistent with established public policy and precedent. On the other hand, public policy favors tort responsibility when a product causes personal injury or other property damage, notwithstanding contractual terms to the contrary.³⁴

28. *State Farm*, 225 Wis. 2d at 321, 592 N.W.2d at 207.

29. *Id.*

30. RESTATEMENT (THIRD) OF TORTS: PRODUCTS LIABILITY § 21 (1998).

31. *But see* *Ins. Co. of N. Am. v. Cease Elec. Inc.*, 2004 WI 139, ¶ 52, 276 Wis. 2d 361, ¶ 52, 688 N.W.2d 462, ¶ 52 (holding that the economic loss doctrine does not apply to contracts for services). *See also* John D. Finerty, Jr. & Charles J. Crueger, *A Commentary on the Economic Loss Doctrine Under the Rule of Cease Electric and Cascade Stone*, 89 MARQ. L. REV. 137 (2005) (criticizing the decision to exempt service contracts from application of the economic loss doctrine).

32. RESTATEMENT (SECOND) OF CONTRACTS § 195 cmt. a (1981).

33. *See* *Kaloti Enters., Inc. v. Kellogg Sales Co.*, 2005 WI 111, ¶ 48, 283 Wis. 2d 555, ¶ 48, 699 N.W.2d 205, ¶ 48.

34. U.C.C. § 2-719(3) (1962); WIS. STAT. § 402.719(3) (2005–2006); *Wausau Tile, Inc. v. County Concrete Corp.*, 226 Wis. 2d 235, 248, 593 N.W.2d 445, 452 (1999).

IV. THE GENESIS AND GROWTH OF THE ECONOMIC LOSS DOCTRINE IN WISCONSIN

The Wisconsin Supreme Court first recognized the economic loss doctrine in 1989.³⁵ In *Sunnyslope Grading, Inc.*, two commercial parties entered into a contract for the sale of a machine.³⁶ The contract contained warranties and limitation of remedies as provided by the Uniform Commercial Code ("U.C.C."). Subsequently, the machine developed problems, and the buyer sought consequential damages. The contract, however, expressly precluded the recovery of consequential damages.³⁷ As a result, the buyer sued in tort to avoid the contractual limitations. The Supreme Court concluded that "a commercial purchaser of a product cannot recover solely economic losses" in tort where the parties have negotiated a contract that defines the buyer's remedies.³⁸

A number of rationales are used to support the decision that prevents a tort action from circumventing the contract. One, of course, is to honor the contract. Theoretically, each party has negotiated the best terms available through their mutual promises, and absent some superseding reason, each should receive the benefit of their bargain. Another rationale is that the U.C.C. is a carefully constructed legislative framework that governs transactions in machines (goods), and tort law should not be used to undermine the U.C.C.'s application. The reasons often stated by the Wisconsin Supreme Court are: (1) to "maintain[] the fundamental distinction between tort law and contract law"; (2) to protect commercial parties' freedom to allocate economic risk by contract; and (3) to encourage the party best situated to assess the risk of economic loss, the commercial buyer, to "assume, allocate, or insure against" that risk.³⁹ Unquestionably, these are strong rationales that supported the Wisconsin Supreme Court's adoption of the economic loss doctrine.⁴⁰

35. *Sunnyslope Grading, Inc. v. Miller, Bradford & Risberg, Inc.*, 148 Wis. 2d 910, 916, 437 N.W.2d 213, 215 (1989).

36. *Id.* at 912-13, 437 N.W.2d at 214.

37. *Id.* at 914, 437 N.W.2d at 214.

38. *Id.* at 921, 437 N.W.2d at 217-18.

39. *Kaloti Enters., Inc. v. Kellogg Sales Co.*, 2005 WI 111, ¶¶ 46, 48, 50, 283 Wis. 2d 555, ¶¶ 46, 48, 50, 699 N.W.2d 205, ¶¶ 46, 48, 50 (quoting *Daanen & Janssen, Inc. v. Cedarapids, Inc.*, 216 Wis. 2d 395, 410, 573 N.W.2d 842, 849 (1997)).

40. The United States Supreme Court also adopted the economic loss doctrine in *East River Steamship Corp. v. Transamerica Delaval, Inc.*, 476 U.S. 858, 874-75 (1986).

The economic loss doctrine has landed in fertile ground in Wisconsin. The doctrine's humble origin was a dispute over a defective "product" between "commercial parties" that resulted in a tort barrier in a U.C.C. case.⁴¹ Notably, the doctrine has three components that could have been used to curtail its growth. First, the doctrine was limited to a "product"⁴² or more specifically a "good."⁴³ Second, the transaction was between commercial parties. And third, the doctrine was applied to a U.C.C. case where Article 2⁴⁴ has detailed and explicit rules that govern the parties' transaction. In all three areas the doctrine's scope has been expanded.

The definition of a product has been expanded from a good to also include real property, including a new home⁴⁵ and a forty-two unit condominium complex.⁴⁶ The doctrine's coverage has increased from applying to commercial transactions to also include consumer transactions.⁴⁷ Finally, the doctrine has been expanded beyond U.C.C. disputes to any contract dispute involving a product.⁴⁸

The growth of the economic loss doctrine has not been limited to simply expanding its three components. The scope of the economic loss doctrine has also been expanded by limiting the traditional areas of tort coverage. A corollary of the economic loss doctrine is that if a defective product causes personal injury or other property damage, then tort theories are available to the aggrieved party. However, two exceptions to the "other property" provision have further limited tort availability and thereby expanded the scope of the economic loss doctrine.

The first exception is the "integrated systems" exception. The integrated systems exception provides that damage by a defective product that is a component of an integrated system, to either the

41. *Sunnyslope*, 148 Wis. 2d at 916, 437 N.W.2d at 215.

42. RESTATEMENT (THIRD) OF TORTS: PRODUCTS LIABILITY § 19 (1998).

43. U.C.C. § 2-105 (1962); Wis. STAT. § 402.105(b)-(c) (2005-2006).

44. Wis. STAT. §§ 402.101-725 (2005-2006).

45. *Linden v. Cascade Stone Co.*, 2005 WI 113, ¶ 25, 283 Wis. 2d 606, ¶ 25, 699 N.W.2d 189, ¶ 25.

46. *1325 N. Van Buren, LLC v. T-3 Group, Ltd.*, 2006 WI 94, ¶ 67, 293 Wis. 2d 410, ¶ 67, 716 N.W.2d 822, ¶ 67.

47. *State Farm Mut. Auto. Ins. Co. v. Ford Motor Co.*, 225 Wis. 2d 305, 324, 592 N.W.2d 201, 209 (1999).

48. *Kaloti Enters., Inc. v. Kellogg Sales Co.*, 2005 WI 111, ¶ 27, 283 Wis. 2d 555, ¶ 27, 699 N.W.2d 205, ¶ 27; *Van Lare v. Vogt, Inc.*, 2004 WI 110, ¶¶ 19-20, 274 Wis. 2d 631, ¶¶ 19-20, 683 N.W.2d 46, ¶¶ 19-20; *Stoughton Trailers, Inc. v. Henkel Corp.*, 965 F. Supp. 1227, 1233 (W.D. Wis. 1997).

system or other system components, is not damage to other property.⁴⁹ Thus, tort theories are not available to the aggrieved party.

The second exception is the “disappointed performance expectations” exception. This exception provides that other property has also not been damaged when the “prevention of the subject risk was one of the contractual expectations motivating the purchase of the defective product.”⁵⁰ In other words, if a defective product causes other property damage, but the damage could have been within the scope of the bargaining, it does not qualify as other property damage. The net effect of both exceptions to the other property provision is to expand the coverage of the economic loss doctrine and to curtail the application of tort principles. In a final expansion, the economic loss doctrine has been applied to circumstances where there was no contract between the parties⁵¹ and solely economic losses were incurred.

There have been some limits, however, placed on the economic loss doctrine. The most significant limitation is that it does not apply to contracts where the primary purpose is to provide services.⁵² The courts use the “predominant” test to determine whether the contract predominantly involves providing a service or the sale of a product.⁵³ Another limitation is the “public safety” exception. The public safety exception provides that where a product has an intrinsic health hazard, tort theories are available to the aggrieved party even though only economic losses have been incurred.⁵⁴ The public safety exception, however, has not been used other than for one case of installing asbestos in a shopping center.⁵⁵ Other than the two limitations noted above, the economic loss doctrine has been greatly expanded by the Wisconsin Supreme Court. Wisconsin now has one of the broadest coverages in the United States.

49. *Wausau Tile, Inc. v. County Concrete Corp.*, 226 Wis. 2d 235, 245, 593 N.W.2d 445, 452 (1999).

50. *Grams v. Milk Prods., Inc.*, 2005 WI 112, ¶ 43, 283 Wis. 2d 511, ¶ 43, 699 N.W.2d 167, ¶ 43 (quoting *Rich Prods. Corp. v. Kemutec, Inc.*, 66 F. Supp. 2d 937, 975 (E.D. Wis. 1999)).

51. *Linden v. Cascade Stone Co.*, 2005 WI 113, ¶ 17, 283 Wis. 2d 606, ¶ 17, 699 N.W.2d 189, ¶ 17.

52. *Ins. Co. of N. Am. v. Cease Elec. Inc.*, 2004 WI 139, ¶ 52, 276 Wis. 2d 361, ¶ 52, 688 N.W.2d 462, ¶ 52. *But see* *Finerty & Crueger*, *supra* note 31 (criticizing the *Cease* decision).

53. *Linden*, 2005 WI 113, ¶ 8, 283 Wis. 2d 606, ¶ 8, 699 N.W.2d 189, ¶ 8.

54. *Northridge Co. v. W.R. Grace & Co.*, 162 Wis. 2d 918, 937–38, 471 N.W.2d 179, 186 (1991).

55. *See Northridge*, 162 Wis. 2d at 922, 937–38, 471 N.W.2d at 180, 186; *see also* *Wausau Tile, Inc. v. County Concrete Corp.*, 226 Wis. 2d 235, 264–65, 593 N.W.2d 445, 458–59 (1999) (rejecting the public safety exception).

V. IDENTIFYING ECONOMIC LOSSES

The tipping point between contract and tort under the economic loss doctrine is the type of damages suffered. If a defective product causes solely economic loss then contract law controls. On the other hand, if a defective product causes personal injury or other property damage, then tort law controls. Thus, it is critical to be able to identify solely economic losses. Economic losses are those damages that arise whenever the product does not perform as agreed, "including damage to the product itself or monetary losses caused by the product."⁵⁶ Economic losses include the difference in value between what is received and the value as represented;⁵⁷ the cost of repair or replacement;⁵⁸ lost profits;⁵⁹ the costs of paying third party claims as a result of the defective product;⁶⁰ and any other losses that are not personal injury or other property damage.⁶¹

VI. THE FRAUD IN THE INDUCEMENT EXCEPTION TO THE ECONOMIC LOSS DOCTRINE

Fraud in the inducement is "when a misrepresentation leads another to enter into a transaction with a false impression of the risks, duties, or obligations involved."⁶² In general, courts have taken three approaches when fraud is used to induce one to enter into a contract and solely economic losses are incurred.⁶³ The first approach is to ignore the fraud and the defrauded party's remedy is solely contract, not tort.⁶⁴ The second approach is a broad exception that recognizes the fraud as a tort in all cases of fraudulent inducement.⁶⁵ The defrauded party is free to

56. *Linden*, 2005 WI 113, ¶ 6, 283 Wis. 2d 606, ¶ 6, 699 N.W.2d 189, ¶ 6.

57. *Northridge*, 162 Wis. 2d at 926, 471 N.W.2d at 182.

58. *Id.*, 471 N.W.2d at 182; *State Farm Mut. Auto. Ins. Co. v. Ford Motor Co.*, 225 Wis. 2d 305, 343, 592 N.W.2d 201, 216 (1999); *Wausau Tile, Inc.*, 226 Wis. 2d at 248, 593 N.W.2d at 452.

59. *Wausau Tile, Inc.*, 226 Wis. 2d at 257, 593 N.W.2d at 455; *Northridge*, 162 Wis. 2d at 926, 471 N.W.2d at 182; 1325 N. Van Buren, LLC v. T-3 Group, Ltd., 2006 WI 94, ¶ 24, 293 Wis. 2d 410, ¶ 24, 716 N.W.2d 822, ¶ 24.

60. *Wausau Tile, Inc.*, 226 Wis. 2d at 253, 593 N.W.2d at 454.

61. 1325 N. Van Buren, 2006 WI 94, ¶ 24, 293 Wis. 2d 410, ¶ 24, 716 N.W.2d 822, ¶ 24; *State Farm*, 225 Wis. 2d at 320, 592 N.W.2d at 207.

62. BLACK'S LAW DICTIONARY 686 (8th ed. 2004).

63. *Kaloti Enters., Inc. v. Kellogg Sales Co.*, 2005 WI 111, ¶ 31, 283 Wis. 2d 555, ¶ 31, 699 N.W.2d 205, ¶ 31.

64. *Id.* ¶ 31, 283 Wis. 2d 555, ¶ 31, 699 N.W.2d 205, ¶ 31.

65. *Id.*, 283 Wis. 2d 555, ¶ 31, 699 N.W.2d 205, ¶ 31.

seek a remedy in tort. Seven states have adopted the broad exception,⁶⁶ and federal courts have indicated that thirteen other states will likely adopt it.⁶⁷ The rationale of the broad approach is that the deceitful

66. ALABAMA: *Ford Motor Co. v. Rice*, 726 So. 2d 626, 631 (Ala. 1998) (stating that the court has often allowed fraudulent inducement claims for economic loss from misrepresented value of a product, even when the product was working properly). CALIFORNIA: *Robinson Helicopter Co. v. Dana Corp.*, 102 P.3d 268, 274 (Cal. 2004) (citing *Erlich v. Menezes*, 981 P.2d 978, 983 (Cal. 1999)) (stating that tort damages have been allowed in contract cases for fraudulent inducement). COLORADO: *Town of Alma v. Azco Constr., Inc.*, 10 P.3d 1256, 1263–64 (Colo. 2000) (stating that the economic loss rule does not apply to claims arising from a duty independent of contract and that common law fraud is an independent duty); *United Int'l Holdings, Inc. v. Wharf (Holdings) Ltd.*, 210 F.3d 1207, 1227 (10th Cir. 2000) (finding that Colorado's economic loss rule only applies to some forms of negligence). HAWAII: *State v. U.S. Steel Corp.*, 919 P.2d 294, 302 (Haw. 1996) (stating that the economic loss doctrine does not apply to claims of negligent misrepresentation or fraud). ILLINOIS: *Moorman Mfg. Co. v. Nat'l Tank Co.*, 435 N.E.2d 443, 452 (Ill. 1982) (stating that economic loss is recoverable when false representations are made); *Faust Printing, Inc. v. MAN Capital Corp.*, No. 02-C-9345, 2006 U.S. Dist. LEXIS 44140, at *20 (N.D. Ill. June 16, 2006) (finding the fraudulent misrepresentation exception from *Moorman* is still viable). NEBRASKA: *Streeks, Inc. v. Diamond Hill Farms, Inc.*, 605 N.W.2d 110, 123 (Neb. 2000) (stating that a purchaser is not limited to contract and may bring an action for fraudulent misrepresentation as well). TEXAS: *Formosa Plastics Corp. USA v. Presidio Eng'rs & Contractors*, 960 S.W.2d 41, 47 (Tex. 1998) (holding that damages can be recovered for fraudulent inducement even when misrepresentations concern the subject matter of the contract).

67. IOWA: *Cunningham v. PFL Life Ins. Co.*, 42 F. Supp. 2d 872, 887 (N.D. Iowa 1999) (predicting that Iowa would adopt a broad fraud exception and not follow Florida's narrow exception). MASSACHUSETTS: *Arthur D. Little Int'l, Inc. v. Dooyang Corp.*, 928 F. Supp. 1189, 1192 (D. Mass. 1996) (stating that "[t]he economic loss rule does not apply to intentional misrepresentations"). MARYLAND: *Superior Bank, F.S.B. v. Tandem Nat'l Mortgage, Inc.*, No. MJG-99-2360, 2000 U.S. Dist. LEXIS 22224, at *8 (D. Md. May 12, 2000) (stating that when "misrepresentations induce [a party] to enter into a contract, the economic loss rule does not apply"). MINNESOTA: *Lester Bldg. Sys. v. Louisiana-Pacific Corp.*, No. A03-48, 2004 Minn. App. LEXIS 156, at *16–*18 (Minn. Ct. App. Feb. 17, 2004) (finding that federal cases interpreting Minnesota law did not consider the recent amendment to the economic loss statute and that the fraud exemption does not mention anything about needing to be extraneous of the contract). NEBRASKA: *Accurate Commc'ns, LLC v. Startel Corp.*, No. 4:05CV3286, 2006 U.S. Dist. LEXIS 11232, at *9–10 (D. Neb. Feb. 28, 2006) (finding that Nebraska law will allow a plaintiff to bring a breach of contract and misrepresentation action simultaneously). NEVADA: *Yerington Ford, Inc. v. Gen. Motors Acceptance Corp.*, 359 F. Supp. 2d 1075, 1083–84 (D. Nev. 2004) (noting that tort claims will be barred when not independent of contractual duties, but fraud in the inducement is always extraneous of the contract). NEW JERSEY: *Bracco Diagnostics, Inc. v. Bergen Brunswig Drug Co.*, 226 F. Supp. 2d 557, 563 (D.N.J. 2002) (finding that in New Jersey, fraud must be extraneous to the contract in order to survive the economic loss rule, and noting that fraud in the inducement is generally extraneous to the contract). NEW YORK: *EED Holdings v. Palmer Johnson Acquisition Corp.*, 387 F. Supp. 2d 265, 279 (S.D.N.Y. 2004) (finding it well established in New York law that fraudulent inducement is collateral to the contract and will support a fraud claim). OHIO: *Onyx Envtl. Servs., LLC v. Maison*, 407 F. Supp. 2d 874, 879 (N.D. Ohio 2005) (finding that fraud in the inducement implicates a duty distinct from contractual duties, and thus the economic loss doctrine does not apply). SOUTH CAROLINA: *Enhance-It,*

conduct arouses a sufficient public interest to permit tort principles to apply to remedy the wrong. The third approach is a narrow exception that recognizes the fraud as a tort only where the fraud is not interwoven with the quality or character of the goods or otherwise involves performance of the contract. In other words, the fraud is actionable as a tort only if it is extraneous to the subject matter of the contract. Wisconsin, Florida, and arguably Michigan⁶⁸ are the only states to adopt the narrow exception.⁶⁹ The Wisconsin Supreme Court offered three rationales for adopting the narrow approach.⁷⁰ First, the narrow exception maintains the fundamental distinction between contract and tort law.⁷¹ Matters that are expressly or implicitly dealt with in the contract, such as the performance or quality or character of the goods sold, still must be addressed by the contract. Second, the narrow exception promotes and protects the parties' freedom to contract.⁷² The parties are expected to negotiate with reference to all those matters that one would expect should be addressed in the contract. Third, the narrow exception encourages the party with the best understanding of the attendant risks, the buyer, to assume, allocate,

L.L.C. v. Am. Access Techs., Inc., 413 F. Supp. 2d 626, 634 (D.S.C. 2006) (finding that a party induced into entering a contract has the election of either tort or contract remedies). SOUTH DAKOTA: *N.W. Pub. Serv. v. Union Carbide Corp.*, 115 F. Supp. 2d 1164, 1170 (D.S.D. 2000) (predicting the South Dakota Supreme Court would adopt a broad fraud exception). UTAH: *Associated Diving & Marine Contractors v. Granite Constr. Co.*, No. 2:01CV330DB, 2003 U.S. Dist. LEXIS 21560, at *23 (D. Utah July 10, 2003) (finding a claim for fraud in the inducement cannot be barred by the economic loss doctrine). VIRGINIA: *McKesson Medical-Surgical, Inc. v. A.T. Kearney, Inc.*, 271 F. Supp. 2d 827, 829 (E.D. Va. 2003) (finding that fraud that precedes contract formation does not implicate a contractual duty and that the economic loss rule will not apply); *City of Richmond v. Madison Mgmt. Group, Inc.*, 918 F.2d 438, 446 (4th Cir. 1990) (stating that fraud implicates a tort duty and that the economic loss rule only bars those claims arising from contractual duties).

68. The Michigan Supreme Court has not yet decided amongst the three approaches.

69. FLORIDA: *HTP, Ltd. v. Lineas Aereas Costarricenses, S.A.*, 685 So. 2d 1238, 1239 (Fla. 1996) (finding tort claims must be independent of the contractual obligations or they are barred by the economic loss rule); *Indem. Ins. Co. v. Am. Aviation, Inc.*, 891 So. 2d 532, 542-43 (Fla. 2004). MICHIGAN: *Huron Tool & Eng'g Co. v. Precision Consulting Servs., Inc.*, 532 N.W.2d 541, 546 (Mich. Ct. App. 1995) (finding tort claims must be extraneous from contract matter); *GE Healthcare Fin. Servs. v. Cardiology & Vascular Assocs.*, No. 05-71304, 2006 WL 950268, at *2 (E.D. Mich. Apr. 12, 2006) (holding that plaintiff must show a misrepresentation is "extraneous to the contract"). WISCONSIN: *Kaloti Enters., Inc. v. Kellogg Sales Co.*, 2005 WI 111, ¶ 42, 283 Wis. 2d 555, ¶ 42, 699 N.W.2d 205, ¶ 42 (finding fraud in the inducement will be barred by the economic loss doctrine unless extraneous to the contract).

70. *Kaloti*, 2005 WI 111, ¶¶ 46, 48, 50, 283 Wis. 2d 555, ¶¶ 46, 48, 50, 699 N.W.2d 205, ¶¶ 46, 48, 50.

71. *Id.* ¶ 46, 283 Wis. 2d 555, ¶ 46, 699 N.W.2d 205, ¶ 46.

72. *Id.* ¶ 48, 283 Wis. 2d 555, ¶ 48, 699 N.W.2d 205, ¶ 48.

or insure against the risk of fraud on interwoven terms.⁷³ Federal courts have indicated that five other states will likely adopt the narrow exception.⁷⁴ Some states have not given any indication whether a fraud in the inducement exception to the economic loss doctrine will be recognized.⁷⁵

The narrow fraud in the inducement exception requires the aggrieved party to establish: (1) that all the elements of intentional misrepresentation are present;⁷⁶ (2) that the intentional misrepresentation occurred prior to contract formation; and (3) that the fraud relates to a matter extraneous to the contract.⁷⁷ The narrow exception requires the court to draw a distinction between those matters that are interwoven with the contract and those that are extraneous. Only the concept of interwoven is defined.

73. *Id.* ¶ 50, 283 Wis. 2d 555, ¶ 50, 699 N.W.2d 205, ¶ 50.

74. ARIZONA: *QC Constr. Prods., LLC v. Cohill's Bldg. Specialties, Inc.*, 423 F. Supp. 2d 1008, 1015–16 (D. Ariz. 2006) (finding that fraud claims are barred by the economic loss doctrine as not distinct from breach of contract). DELAWARE: *Pinkert v. John J. Olivieri, P.A.*, No. 99-380-SCR, 2001 U.S. Dist. LEXIS 8133, at *18 (D. Del. May 24, 2001) (finding that fraud claims will be barred by economic loss doctrine if not contingent on duties outside of contract); *In re Crown-Simplimatic Inc.*, 299 B.R. 319, 324 (Bankr. D. Del. 2003) (holding that fraud in the inducement claim was barred by the economic loss doctrine as the violated rights were encompassed in contract). KENTUCKY: *Strathmore Web Graphics v. Sanden Mach., Ltd.*, No. 3:99CV-345-S, 2000 U.S. Dist. LEXIS 22618, at *9–10 (W.D. Ky. May 16, 2000) (holding that fraud in the inducement claim was barred by the economic loss doctrine as the fraud was not distinct from breach of contract or warranty claims). *But cf.* *Davis v. Siemens Med. Solutions USA, Inc.*, 399 F. Supp. 2d 785, 801 (W.D. Ky. 2005) (refusing to bar a fraud in the inducement claim stemming from an employment contract without guidance from Kentucky courts). MISSOURI: *Self v. Equilon Enters., LLC*, No. 4:00CV1903 TIA, 2005 U.S. Dist. LEXIS 17288, at *40 (E.D. Mo. Mar. 30, 2005) (predicting that the Missouri Supreme Court would hold that the economic loss rule would bar all fraud claims that were not independent of the contract). PENNSYLVANIA: *Werwinski v. Ford Motor Co.*, 286 F.3d 661, 680 (3d Cir. 2002) (predicting that the Supreme Court of Pennsylvania would find that the economic loss doctrine would bar intentional torts, but that fraud in the inducement will be an exception if extraneous to the subject matter of the contract); *Lake St. Gaming, LLC v. IGames Entm't, Inc.*, No. 04-4965, 2006 U.S. Dist. LEXIS 38141, at *8, *10 (E.D. Pa. June 8, 2006) (requiring fraud in the inducement claim to be based on facts not embodied in contract); *Air Prods. & Chems., Inc. v. Eaton Metal Prods. Co.*, 256 F. Supp. 2d 329, 337 (E.D. Pa. 2003) (following *Werwinski*, stating that even if the Pennsylvania Supreme Court applied the economic loss doctrine to bar fraud claims, fraud in the inducement would be allowed if extraneous to subject matter of the contract).

75. These states include Alaska, Connecticut, Georgia, Idaho, Indiana, Kansas, Louisiana, Maine, Mississippi, New Hampshire, New Mexico, North Carolina, North Dakota, Oklahoma, Oregon, Rhode Island, Tennessee, Vermont, West Virginia, and Wyoming.

76. Wis. JI–Civil 2401 (2005) (misrepresentation: intentional deceit).

77. *Kaloti*, 2005 WI 111, ¶ 42, 283 Wis. 2d 555, ¶ 42, 699 N.W.2d 205, ¶ 42.

Interwoven contract terms arise in two different ways. The first is terms that relate to the quality or character of the product that is the subject matter of the contract.⁷⁸ Those terms that relate to the quality or character of the product are further defined as either: (1) expressly dealt with in the contract, or (2) relating to the "reasonable expectations of the parties to the risk of loss in the event the goods purchased did not meet the purchaser's expectations."⁷⁹ The second way interwoven contract terms arise is in matters that involve performance under the contract.⁸⁰ No definition is provided to identify those matters that involve performance under the contract. More importantly, the decision to distinguish interwoven terms and extraneous terms is a murky one. Even for those few states that have adopted the narrow exception, the guidance is uneven.

In Wisconsin, the supreme court adopted the narrow fraud in the inducement exception in *Kaloti v. Kellogg Enterprises Inc.*⁸¹ In *Kaloti*, a food wholesaler brought an action against a cereal company and its representative for damages it incurred as a result of Kellogg's failure to disclose a change in the company's marketing strategy.⁸² The contract was for the sale of food products that Kaloti intended to resell to retailers. At the time of the contract, Kellogg had also decided to sell directly to the same retailers, but it did not disclose that fact to Kaloti. The court concluded that Kellogg's failure to disclose the change in marketing strategy was an intentional misrepresentation.⁸³ Further, the court concluded that the intentional misrepresentation was extraneous to, not interwoven with, the contract. The court reasoned that the misrepresentation did not regard the quality or character of the product sold or performance under the contract. "Rather, the alleged misrepresentation concerned a matter whose risk was never contemplated to be a part of the contract to purchase Kellogg's products."⁸⁴

It is difficult to see how Kellogg's decision to sell directly to Kaloti's customers is not a matter involving performance under the contract or otherwise interwoven in the sale of the product. Obviously, this is a difficult decision to make. Little guidance is provided from the other

78. *Id.* ¶ 43, 283 Wis. 2d 555, ¶ 43, 699 N.W.2d 205, ¶ 43.

79. *Id.*, 283 Wis. 2d 555, ¶ 43, 699 N.W.2d 205, ¶ 43.

80. *Id.* ¶ 42, 283 Wis. 2d 555, ¶ 42, 699 N.W.2d 205, ¶ 42.

81. *Id.*, 283 Wis. 2d 555, 699 N.W.2d 205.

82. *Id.* ¶ 6, 283 Wis. 2d 555, ¶ 6, 699 N.W.2d 205, ¶ 6.

83. *Id.* ¶ 52, 283 Wis. 2d 555, ¶ 52, 699 N.W.2d 205, ¶ 52.

84. *Id.* ¶ 45, 283 Wis. 2d 555, ¶ 45, 699 N.W.2d 205, ¶ 45.

states that have adopted the narrow exception. In Michigan, no cases have been decided to illustrate those terms that are extraneous to the subject matter. In Florida, the cases decided after the Florida Supreme Court adopted the narrow exception⁸⁵ are perplexing. In *Allen v. Stephan Co.*, the seller of a business made representations that the business "had paid its taxes, filed all necessary tax returns and that the company's financial statements accurately disclosed all of its liabilities."⁸⁶ The representations were incorporated into the sales agreement. The Florida Court of Appeals held that the fraud claim was not barred by the economic loss doctrine even though the fraudulent inducement related to matters included in the contract.⁸⁷ Similarly, in *La Pesca Grande Charters v. Moran*, the seller of a yacht made representations that its engines were recently rebuilt, that the hull was sound, and that the fire extinguisher system was operational.⁸⁸ The representations were false, and the buyer sued for fraud. The trial court dismissed the fraud claim.⁸⁹ The Florida District Court of Appeals, however, reversed. The buyer was permitted to pursue its fraud claim though the representations unquestionably were interwoven terms.⁹⁰ Clearly, the narrow exception has only been marginally adopted and is difficult to apply.

VII. CONTRACT PRINCIPLES AND FRAUD

A. The "As Is" Clause and Fraud

The narrow fraud in the inducement exception clearly contradicts the well-established principle that fraudulent conduct is punished as a tort despite a clause in the party's contract that may provide otherwise. An "as is" clause is a common clause used in the sale of a property. Essentially "[a]n 'as is' clause puts the burden on the buyer . . . to determine the condition of the property being purchased."⁹¹ This is essentially the same as the third rationale used by the Wisconsin Supreme Court in adopting the narrow exception, which is to encourage

85. *HTP, Ltd. v. Lineas Aereas Costarricenses, S.A.*, 685 So. 2d 1238, 1239 (Fla. 1996).

86. 784 So. 2d 456, 457 (Fla. Dist. Ct. App. 2000).

87. *Id.* at 458.

88. 704 So. 2d 710, 712 (Fla. Dist. Ct. App. 1998).

89. *Id.*

90. *Id.*

91. *McCabe v. Midwest Evergreens, Inc.* No. 95-2148, 1996 WL 118456, at *1 (Wis. Ct. App. Mar. 19, 1996); see *Fulton v. Vogt*, No. 96-1972, 1998 WL 313409, at *2 (Wis. Ct. App. June 16, 1998).

the party with the best understanding of the attendant risks, the buyer, to assume, allocate, and insure against the risk.⁹² An as is clause is a complete disclaimer of any implied warranties.⁹³ Further, the seller has no duty to investigate where the contract contains an as is clause.⁹⁴ If property is sold as is and there is no fraud in the process, the clause is effective.⁹⁵ On the other hand, once fraud is introduced into the process, the contract clause is no longer effective. The as is clause does not protect one from a lawsuit based on one's intentional misrepresentation.⁹⁶ The courts have clearly indicated that one's fraud supersedes the negotiated contract terms. Public policy dictates that a deceitful person cannot hide behind an as is clause in a contract. The fraud is actionable under tort law despite the contract clause negotiated between the parties.⁹⁷ The rationale underlying the courts' decisions is clear. The seller, not the buyer, is the party best able to understand the attendant risks in the transaction. The seller is introducing fraud into the transaction. Focusing tort liabilities on the seller is the most effective way to insure against deceitful conduct by sellers in the future. Requiring the buyer to protect himself against the seller's fraud is pressure applied at the wrong point. The courts have recognized this principle when as is clauses and fraud have conflicted in the past. The courts have not required a buyer to protect himself in a contract against a seller's deceitful conduct as the *Kellogg* decision requires.

B. The Parol Evidence Rule and Fraud

The narrow fraud in the inducement exception to the economic loss doctrine completely undercuts the policy and rationale for creating the fraud exception to the parol evidence rule. The parol evidence rule provides that prior or contemporaneous evidence is not admissible to vary or contradict the terms of a written contract that is final and complete.⁹⁸ The rule is also stated that a "completely integrated

92. See *Kaloti Enters., Inc. v. Kellogg Sales Co.*, 2005 WI 111, ¶ 50, 283 Wis. 2d 555, ¶ 50, 699 N.W.2d 205, ¶ 50.

93. U.C.C. § 2-316(3) (1998); WIS. STAT. § 402.316(3) (2005-2006).

94. *Chapman v. Mut. Serv. Cas. Ins. Co.*, 35 F. Supp. 2d 699, 708 (E.D. Wis. 1999).

95. *Raskin v. Chrysler Realty Corp.*, No. 93-1218, 1994 WL 621954, at *4-*5 (Wis. Ct. App. Nov. 8, 1994); *Omernik v. Bushman*, 151 Wis. 2d 299, 303, 444 N.W.2d 409, 411 (Ct. App. 1989).

96. *McCabe*, 1996 WL 118456, at *1; *Grube v. Daun*, 173 Wis. 2d 30, 49, 496 N.W.2d 106, 112 (Ct. App. 1992).

97. *McCabe*, 1996 WL 118456, at *1; *Grube*, 173 Wis. 2d at 62, 496 N.W.2d at 118.

98. WIS. STAT. § 402.202 (2005-2006).

agreement discharges prior agreements to the extent that they are within its scope."⁹⁹ The rule is a substantive rule of contract law, not evidence.¹⁰⁰ Frequently, parties use an integration or merger clause to maximize the impact of the parol evidence rule. An integration or merger clause is "[a] contractual provision stating that the contract represents the parties' complete and final agreement and supersedes all informal understandings and oral agreements relating to the subject matter of the contract."¹⁰¹ Thus, the contract consists of only the written terms, and nothing extraneous can be considered to add to or vary the written contract. The extrinsic evidence barred by the parol evidence rule are those terms that reasonably¹⁰² or certainly¹⁰³ would have been included in the written contract. The parol evidence rule essentially precludes the admissibility of interwoven terms.

The parol evidence rule as stated in the U.C.C. is silent on whether prior or contemporaneous evidence of fraud can be admitted to prove the tort of intentional misrepresentation despite the existence of a contract that is final and complete.¹⁰⁴ Nevertheless, the U.C.C. cases do permit a tort suit for intentional misrepresentation, despite the parol evidence rule or an integration clause.¹⁰⁵ The Restatement (Second) of Contracts, on the other hand, expressly recognizes fraud as an exception to the parol evidence rule.¹⁰⁶ The courts have uniformly recognized the fraud exception to the parol evidence rule despite a party's failure to read the contract,¹⁰⁷ a signed disclaimer,¹⁰⁸ or an integration clause.¹⁰⁹ In making the decision whether to admit evidence of fraud in the face of the parol evidence rule, the courts have had to weigh the advantage of contract certainty against the harm that would result from fraud. The courts have concluded that the better public policy is to abandon the

99. RESTATEMENT (SECOND) OF CONTRACTS § 213(2) (1981).

100. *Id.* § 213 cmt. 1; *H & M Italian Food Corp. v. Gen. Growth Dev. Corp.*, No. 88-1257, 1989 WL 53664, at *2 (Wis. Ct. App. Mar. 21, 1989).

101. BLACK'S LAW DICTIONARY 824 (8th ed. 2004).

102. RESTATEMENT (SECOND) OF CONTRACTS § 209(3) (1981).

103. U.C.C. § 2-202 cmt. 3 (1962).

104. *Id.*

105. *Franklin v. Lovitt Equip.*, 420 So. 2d 1370, 1372 (Miss. 1982); *George Robberecht Seafood, Inc. v. Maitland Bros. Co.*, 255 S.E.2d 682, 683 (Va. 1979); *Cone Mills Corp. v. A.G. Estes, Inc.*, 377 F. Supp. 222, 225 (N.D. Ga. 1974).

106. RESTATEMENT (SECOND) OF CONTRACTS § 214 (1981).

107. *Bank of Sun Prairie v. Esser*, 155 Wis. 2d 724, 732-33, 456 N.W.2d 585, 589 (1990).

108. *State v. Keehn*, 74 Wis. 2d 218, 225, 246 N.W.2d 547, 551 (1976).

109. *See Anderson v. Tri-State Home Improvement Co.*, 268 Wis. 455, 459, 67 N.W.2d 853, 857 (1955).

contract position in favor of redressing the wrong committed by the fraud.¹¹⁰ The same public policy that sanctions the promises obtained by deceit must avoid all attempts to circumvent that policy by means of any contractual devices, including the parol evidence rule. For courts to rule otherwise would open the door to a multitude of frauds that would be hidden behind the parol evidence rule. The parol evidence rule was designed to prevent fraud, not to be used to perpetrate fraud.¹¹¹

The clear policy is to admit any evidence of intentional misrepresentation, despite the parol evidence rule. Upon proof of the fraud, punitive damages are often awarded against the tortfeasor.¹¹² Paradoxically, a situation may now occur in a contract setting where the fraud exception to the parol evidence rule could be used to admit evidence of interwoven terms, but the fraud would not be actionable as a tort under the narrow exception to the economic loss doctrine because the fraud relates to interwoven terms. The point of the fraud exception to the parol evidence rule is to punish the deceitful tortfeasor, which, of course, will always be defeated by the narrow exception to the economic loss doctrine.

C. Contract Disclaimers and Exculpatory Clauses

The narrow fraud in the inducement exception is against public policy because it permits a deceitful person to accomplish indirectly that which the person could not accomplish directly through the party's contract. Freedom of contract generally leads a court to conclude that exculpatory clauses and disclaimers, if fairly bargained, should be enforced.¹¹³ On the other hand, tort principles generally cause a court to be reluctant to shift the burden from the tortfeasor to the victim who has no control or responsibility for the offending conduct. Exculpatory clauses, however, can exempt one from liability for negligent behavior under prescribed circumstances.¹¹⁴ As a result, one party insulates himself from liability for his negligence.¹¹⁵ Such contractual provisions

110. *Id.* at 460, 67 N.W.2d at 857.

111. *H & M Italian Food Corp. v. Gen. Growth Dev. Corp.*, No. 88-1257, 1989 WL 53664, at *2 (Wis. Ct. App. Mar. 21, 1989).

112. *See id.* at *5.

113. *Atkins v. Swimwest Family Fitness Ctr.*, 2005 WI 4, ¶ 25, 277 Wis. 2d 303, ¶ 25, 691 N.W.2d 334, ¶ 25; *Disc. Fabric House of Racine, Inc. v. Wis. Tel. Co.*, 117 Wis. 2d 587, 600, 345 N.W.2d 417, 423 (1984).

114. *Atkins*, 2005 WI 4, ¶¶ 15, 17, 25, 277 Wis. 2d 303, ¶¶ 15, 17, 25, 691 N.W.2d 334, ¶¶ 15, 17, 25; *Disc. Fabric House of Racine, Inc.*, 117 Wis. 2d at 591, 345 N.W.2d at 419.

115. RESTATEMENT (SECOND) OF CONTRACTS § 195(2) (1981).

are permitted as acceptable public policy. However, if fraud in the inducement is utilized to induce one to sign the exculpatory clause or disclaimer, then public policy will not permit enforcement of the clauses.¹¹⁶ On the other hand, public policy dictates that "[a] term exempting a party from tort liability for harm caused intentionally or recklessly is unenforceable."¹¹⁷ Wisconsin courts have regularly recognized this principle.¹¹⁸ The principle is grounded in sound public policy that tort law imposes standards of conduct for the protection of the public. Thus, a party should not be able to exempt himself by contract for harm that he or she intentionally or recklessly causes.¹¹⁹ Specifically, a party cannot by contract exculpate himself or herself from the legal consequences of fraud.¹²⁰ Many years ago, the Wisconsin Supreme Court recognized that an express agreement made in a contract that the contract shall be incontestable for fraud is void as against public policy.¹²¹ At least one state has by statute prohibited any contract term that exempts one for responsibility for one's intentional misrepresentation.¹²² Such clauses have also been held to be against public policy in securities fraud litigation where the contract eliminates the liability for any fraudulent misrepresentations in the sale of the securities.¹²³ There is a clear public policy that a party cannot by contract exculpate himself or herself from liability for deceitful conduct. Public policy does not permit the tortfeasor under any circumstances to contract away his responsibility for his deceitful conduct. Yet, the narrow exception to the economic loss doctrine prevents a defrauded party from suing the tortfeasor for the intentional tort committed when the fraud is interwoven with the contract. In other words, the deceitful person is able to accomplish through the narrow exception (immunity from a tort cause of action for deceit) that which one could not

116. *Merten v. Nathan*, 108 Wis. 2d 205, 215, 321 N.W.2d 173, 178 (1982); *Anderson v. Tri-State Home Improvement Co.*, 268 Wis. 455, 460, 67 N.W.2d 853, 857 (1955); *Malas v. Lounsbury*, 193 Wis. 531, 534, 214 N.W. 332, 333 (1927).

117. RESTATEMENT (SECOND) OF CONTRACTS § 195(1) (1981).

118. *Malas*, 193 Wis. at 534, 214 N.W. at 333; *Finch v. Southside Lincoln-Mercury, Inc.*, 2004 WI App 110, ¶ 23, 274 Wis. 2d 719, ¶ 23, 685 N.W.2d 154, ¶ 23; *Atkins*, 2005 WI 4, ¶ 19, 277 Wis. 2d 303, ¶ 19, 691 N.W.2d 334, ¶ 19; *RepublicBank Dallas, N.A. v. First Wis. Nat'l Bank*, 636 F. Supp. 1470, 1474 (E.D. Wis. 1986); *Dobratz v. Thomson*, 161 Wis. 2d 502, 515, 486 N.W.2d 654, 659 (1991).

119. *Finch*, 2004 WI App 110, ¶ 23, 274 Wis. 2d 719, ¶ 23, 685 N.W.2d 154, ¶ 23.

120. RESTATEMENT (SECOND) OF CONTRACTS § 196 (1981).

121. *Malas*, 193 Wis. at 534, 214 N.W. at 333.

122. CAL. CIV. CODE § 1668 (2006) (certain contracts unlawful).

123. *Merzin v. Provident Fin. Group Inc.*, 311 F. Supp. 2d 674, 685 (S.D. Ohio 2004).

accomplish directly through contract by a disclaimer or exculpatory clause. Disclaimers and exculpatory clauses for intentional torts are against public policy. The narrow exception, which provides the same tort immunity for fraud interwoven with the contract, is similarly against public policy.

D. Contract Principles Summary

The narrow exception conflicts with established contract principles in a number of ways. First, in the case of as is clauses in contracts, any fraud or deceit practiced has always taken precedence over such a clause. The fraudulent seller is not permitted to hide behind such a clause, albeit freely and fairly negotiated for likely a lower sales price. The deceit has always been redressed through a tort action. The court's focus has not been to require the buyer to protect himself through the contract. Rather, the court's approach has been to punish the tortfeasor and deter him or her and others who might consider using such misconduct in the future.

Second, the fraud exception to the parol evidence rule was created so that the parol evidence rule would not be used to perpetrate frauds by excluding evidence of one's fraud. Evidence of fraud has always been admissible, despite a written contract that contained an integration clause. Once admitted, the fraudulent conduct has always been actionable under tort law. The narrow exception to the economic loss doctrine, however, conflicts with the policy supporting the creation of the fraud exception to the parol evidence rule. Extrinsic evidence of interwoven fraud that would be admitted under the parol evidence rule to avoid perpetrating a fraud is not actionable as tortious conduct under the narrow exception. Only contract remedies are available.

Finally, contract law generally tolerates an exculpatory clause in a contract that exculpates a party for his or her negligent conduct. On the other hand, contract law has never permitted an exculpatory clause to exculpate one from one's responsibility for intentional misconduct. This has always been prohibited as against public policy. The narrow exception's prohibition against tort liability for intentional misconduct does indirectly what cannot be done directly in the contract. The narrow exception exculpates one from tort responsibility if the deceit is considered to be interwoven fraud. In sum, the narrow exception conflicts with established contract principles and is not sound public policy.

VIII. TORT PRINCIPLES AND FRAUD

A. Promissory Fraud

The narrow fraud in the inducement exception to the economic loss doctrine eliminates the tort of promissory fraud committed in conjunction with a contract for the sale of a product. "A contract is a promise or set of promises" that upon breach the law gives a remedy.¹²⁴ A contractual promise carries with it the implied assertion of the promisor's intent to perform the promise.¹²⁵ If a contractual promise is made without such intent, a fraudulent misrepresentation has occurred that is actionable.¹²⁶ The person misled by the fraudulent misrepresentation "has a cause of action in tort as an alternative . . . and perhaps in some instances in addition to his [or her] cause of action on the contract."¹²⁷

Wisconsin first recognized the tort of promissory fraud in 1938.¹²⁸ Since 1938, on at least two other occasions the Wisconsin Supreme Court has recognized that when a promisor has no intent to perform its contractual promise at the time of contracting, an actionable tort has occurred.¹²⁹ Promissory fraud is similar to fraud in the inducement. At the time of contracting under promissory fraud, the innocent party is induced to enter into the contract by the false promises of the tortfeasor. The promises made by the tortfeasor are false because the promisor has no intention to fulfill them. Similarly, for fraud in the inducement, at the time of contracting, the innocent party is induced to enter into the contract by the false promises of the tortfeasor. Under both doctrines, there is fraudulent inducement, and for promissory fraud, the innocent party has a tort action against the tortfeasor. Certainly all the fraud in promissory fraud is interwoven fraud since it is the contractual promises themselves that are the subject matter of the fraud. Further, it is likely that in virtually all promissory fraud cases, the damages will be economic loss, not personal injury or other property damage. Thus, with the exception of service contracts,¹³⁰ nearly seventy years of

124. RESTATEMENT (SECOND) OF CONTRACTS § 1 (1981).

125. RESTATEMENT (SECOND) OF TORTS § 530 cmt. c (1977).

126. *Id.* § 530.

127. *Id.* § 530 cmt c.

128. *Alropa Corp. v. Flatley*, 226 Wis. 561, 565–66, 277 N.W. 108, 110 (1938).

129. *Hartwig v. Bitter*, 29 Wis. 2d 653, 656–58, 139 N.W.2d 644, 646–48 (1966); *Anderson v. Tri-State Home Improvement Co.*, 268 Wis. 455, 463, 67 N.W.2d 853, 858 (1955).

130. *Ins. Co. of N. Am. v. Cease Elec. Inc.*, 2004 WI 139, ¶ 52, 276 Wis. 2d 361, ¶ 52, 688 N.W.2d 462, ¶ 52; *see Hartwig*, 29 Wis. 2d at 655, 658–59, 139 N.W.2d at 648.

Wisconsin precedent are reversed by the narrow exception to the economic loss doctrine.

B. Fraud in the Factum/Execution

The narrow fraud in the inducement exception to the economic loss doctrine likely eliminates the tort of fraud in the factum (also referred to as fraud in the execution) committed in conjunction with a contract for the sale of a product. The narrow exception mandates that fraud interwoven with the contract or involving the performance of the contract be addressed through contract remedies, not tort. Only fraud extraneous to the contract permits the use of tort remedies. Fraud in the factum/execution is fraud that occurs “when a legal instrument as actually executed differs from the one intended for execution.”¹³¹ The fraud occurs because one party procures a party’s signature to a contract without that party’s knowledge of the true nature of the contract.¹³² The misrepresentation is “to the character or essential terms of a proposed contract.”¹³³ The remedy for fraud in the factum/execution is that no contract is formed. Punitive damages are often imposed for such fraud because of the egregious breach of public policy.¹³⁴

Fraud in the inducement occurs “when a misrepresentation leads another to enter into a transaction with a false impression of the risks, duties, or obligations involved.”¹³⁵ Fraud in the factum/execution is actually a different kind of fraudulent inducement. Rather than fraudulently misrepresenting the risks, duties, or obligations, the tortfeasor misrepresents the nature of the contract. The nature of the contract is clearly fraud that is interwoven with the contract or involves the contract’s performance. Under the narrow exception, this type of fraud would be actionable only through contract remedies. The tort of fraud in the factum/execution is arguably eliminated by the narrow exception.

C. Fraudulently Inducing One Not to Enter into a Contract

The narrow exception’s directive that interwoven fraud is not actionable in tort fails to recognize the independent, public wrong

131. BLACK’S LAW DICTIONARY 686 (8th ed. 2004).

132. See *id.*; see also *Bank of New Glarus v. Swartwood*, 2006 WI App 224, ¶ 43, 725 N.W.2d 944, ¶ 43.

133. RESTATEMENT (SECOND) OF CONTRACTS § 163 cmt a (1981).

134. *Rodriguez v. Horton*, 622 P.2d 261, 265 (N.M. Ct. App. 1980).

135. BLACK’S LAW DICTIONARY 686 (8th ed. 2004).

committed by the seller's deceitful conduct. One who "intentionally and improperly interferes with another's prospective contractual relation" by inducing a third person not to enter into a contract has committed an actionable tort.¹³⁶ This is a statement of public policy. The tort specifically covers the same "products" that are the domain of the economic loss doctrine.¹³⁷ The interference with another's prospective contractual relations must be an improper one. "The nature of the actor's conduct is a chief factor in determining whether the conduct is improper"¹³⁸ An improper interference is specifically defined as one characterized by fraudulent misrepresentation.¹³⁹ One has a public duty not to fraudulently interfere with another's prospective contractual relations. There is no contract between the prospective parties, yet a societal duty is imposed on a predatory third party. The fraud is not tolerated in anticipation of the two parties contracting. Thus, it is clear that fraud is punishable as a tort even without contractual relations and in fact in anticipation of contractual relations. The harm is the intentional interference. The prospective contractual event is the occasion for the commission of the tort. The tort is the intentional interference that is separate and independent of the prospective contract. The societal duty is not to interfere with another's prospective contractual relations. One who breaches that societal duty by fraudulent conduct has committed an actionable tort independent of the prospective contractual relations.

D. Fraudulently Inducing One Not to Perform a Contract

The narrow exception's directive that interwoven fraud is not actionable in tort fails to recognize the public wrong committed by the tortfeasor's deceitful conduct, which is independent of a companion breach of contract action. Tort and contract law also intersect when one party intentionally and improperly induces another not to perform his or her contract. This is also tortious conduct.¹⁴⁰ There is a general duty in society not to intentionally interfere with another's reasonable business expectations.¹⁴¹ The interference must also be an improper one.¹⁴² Historically, fraud has been identified as one of the means of improper

136. RESTATEMENT (SECOND) OF TORTS § 766B (1979).

137. *Id.* § 766B cmt. c.

138. *Id.* § 767 cmt. c.

139. *See id.*

140. *Id.* § 766.

141. *Id.* § 766 cmt. b.

142. *Id.* § 766 cmt. c.

interference.¹⁴³ The tortious interferences are often by inducement¹⁴⁴ and predatory in nature.¹⁴⁵ The fact that the plaintiff has a cause of action for breach of contract does not preclude the plaintiff from maintaining a tort action against the tortfeasor.¹⁴⁶

Wisconsin has adopted this formulation of tortious interference with contract.¹⁴⁷ The use of fraudulent misrepresentation to induce a breach of contract is a wrong against the public.¹⁴⁸ The harm is the intentional interference, which includes fraud. The contract between the parties is the occasion for the tort. The tort is the intentional interference, which is separate and independent from the contract. The public duty is independent from the contract, which contains the private duties. The tortfeasor's fraudulent conduct violates the societal duty not to intentionally interfere with another's business relations, and thus it is actionable as a tort. The tortfeasor's conduct must be punished to deter such future conduct even though the aggrieved party has a companion breach of contract action. Public policy demands such predatory practices be addressed through tort remedies even though the aggrieved party has a breach of contract action against the breaching party.

E. Duress

The narrow fraud in the inducement exception's directive that interwoven fraud is not actionable in tort contradicts well-established tort law that requires equally culpable conduct be treated in the same manner. Duress is "any wrongful act or threat which overcomes the free will of a party."¹⁴⁹ Under tort law, one who forces another into a contractual relationship as a result of an improper threat¹⁵⁰ is subject to liability.¹⁵¹ There is generally a duty among members of society not to forcibly cause another to enter into a contract. Duress is the breach of

143. *Id.* § 766.

144. *Id.* § 766 cmt. k.

145. *Id.* § 766 cmt. c.

146. *Id.* § 766 cmt. v.

147. *Augustine v. Anti-Defamation League of B'nai B'rith*, 75 Wis. 2d 207, 218–21, 249 N.W.2d 547, 553–54 (1977); *Pure Milk Prods. Coop. v. Nat'l Farmers Org.*, 64 Wis. 2d 241, 257–58, 219 N.W.2d 564, 572–73 (1974).

148. *Pure Milk Prods. Coop. v. Nat'l Farmers Org.*, 90 Wis. 2d 781, 804, 280 N.W.2d 691, 702 (1979).

149. BLACK'S LAW DIRECTORY 542 (8th ed. 2004) (quoting JOHN D. CALAMARI & JOSEPH M. PERILLO, LAW OF CONTRACTS, § 9-2, at 337 (3d ed. 1987)).

150. RESTATEMENT (SECOND) OF TORTS § 871 cmt. f (1979); RESTATEMENT (SECOND) OF CONTRACTS § 176 (1981).

151. RESTATEMENT (SECOND) OF TORTS § 871 (1979).

that duty. One who by duress forces another into a contract is subject to rescission of the contract,¹⁵² compensatory damages, and punitive damages.¹⁵³ Wisconsin recognizes all forms of duress, including business, economic, and physical duress.¹⁵⁴ Wisconsin also recognizes that punitive damages are available when one uses duress to force another into a contractual relationship.¹⁵⁵

Under tort law, duress is considered a specie of fraud in which the compulsion takes the place of deceit in causing the injury. The Restatement (Second) of Torts addresses duress and fraud in the same section. "One who intentionally deprives another of [a] legally protected property interest . . . is subject to liability . . . if [the] conduct is generally culpable . . ." ¹⁵⁶ Both fraud¹⁵⁷ and duress¹⁵⁸ are considered to be equally culpable conduct. Both fraud in the inducement and duress cause the creation of a contract. The only difference is the nature of the culpable conduct. Both, however, are tortious. The Restatement (Second) of Torts provides that the remedies for the tort of duress and the tort of fraud are the same.¹⁵⁹ Punitive damages are available for both fraud and duress under the Restatement (Second) of Torts.¹⁶⁰ As a matter of public policy, should there be a difference between cases where one forcibly or fraudulently causes another to enter into a contract? Duress and fraud are torts that both wrongfully induce the formation of a contract. They are equal wrongs of societal duties and are recognized as coincident torts.¹⁶¹ There are no exceptions for any kind of conduct that involves duress. There is no exception for interwoven terms that limit an aggrieved party to solely contract remedies. The breach of duty and societal wrong is independent of the contractual relationship. The contract is simply the occasion for the tort. An aggrieved person who suffers duress has the full range of tort remedies to address the grievous conduct. On the other hand, one who suffers from deceitful conduct that is interwoven with the contract has

152. RESTATEMENT (SECOND) OF CONTRACTS § 175 (1981).

153. RESTATEMENT (SECOND) OF TORTS § 871 cmt. f, illus. 5 (1979).

154. *Mendelson v. Blatz Brewing Co.*, 9 Wis. 2d 487, 494, 101 N.W.2d 805, 809 (1960).

155. *Frankard v. Amoco Oil Co.*, 116 Wis. 2d 254, 267-68, 342 N.W.2d 247, 253 (Ct. App. 1983).

156. RESTATEMENT (SECOND) OF TORTS § 871 (1979).

157. *Id.* § 871 cmt. e.

158. *Id.* § 871 cmt. f.

159. *Id.*

160. *See generally id.* § 870.

161. *Compare id.* § 871 cmt. e, *with id.* § 871 cmt. f.

no tort remedies under the narrow exception to the economic loss doctrine. There should be no exception for fraudulent conduct. The fraud requires independent redress, as all torts require, in order to promote the public good. The narrow exception clearly contradicts well-established law and does not promote the public good.

F. Conversion by Acting Beyond the Scope of the Contract

The narrow fraud in the inducement exception creates immunity for interwoven fraud that cannot be justified by comparison to a parallel situation that also involves an intentional tort that constitutes a breach of contract. A "[c]onversion is an intentional exercise of dominion or control over a chattel which so seriously interferes with the right of another."¹⁶² A negligent interference is not sufficient to be conversion; it must be intentional.¹⁶³ There are a number of ways to commit the tort of conversion. One particular means is where a person "is authorized to make a particular use of a chattel, and uses it in a manner exceeding the authorization."¹⁶⁴ The actor is liable for conversion. This type of conversion frequently arises in cases of a bailment contract.¹⁶⁵ In essence, the gravamen of this tort is an unauthorized use that exceeds the limits of the authorization, so as to constitute a material breach of the contract. The unauthorized use is a clear breach of the contract, and it also constitutes the tort of conversion. The aggrieved party has a claim in both contract and tort.

Wisconsin case law has accepted the principle that an unauthorized use beyond the limits of a contract's authorization is a conversion.¹⁶⁶ In *Heinen v. Home Mutual Casualty Co.*, a dealer's sale of a mobile home in a manner contrary to the parties' contract was held to be a conversion.¹⁶⁷ Despite the fact that the improper sale was a material breach of the contract, the court also recognized the intentional tort.¹⁶⁸ The analysis for an unauthorized use that exceeds the parameters of the parties' contract is virtually identical to the situation that arises from fraudulently inducing one to enter into a contract. In both situations, a material breach of the contract has occurred. In both situations, a

162. RESTATEMENT (SECOND) OF TORTS § 222A(1) (1965).

163. *Id.* § 224.

164. *Id.* § 228.

165. *Id.* § 228 cmt. a.

166. *Heinen v. Home Mut. Cas. Co.*, 5 Wis. 2d 282, 289, 92 N.W.2d 836, 840 (1958).

167. *Id.*, 92 N.W.2d at 840.

168. *Id.* at 290, 92 N.W.2d at 840.

separately identifiable tort has also occurred. In the case of the conversion, the aggrieved party has an actionable tort claim, notwithstanding a parallel breach of contract claim. In the case of the fraudulent inducement, there is an actionable fraud claim only if the fraud relates to an extraneous matter to the contract. For fraud that relates to the terms of the contract or the contract's performance, no tort is actionable under the narrow exception. This disparate treatment cannot be justified. Surely, deceitful conduct that induces a contract is as reprehensible as a matter of public policy as exceeding a contractually authorized use. Further, the unauthorized use is by definition a dispute that relates to an interwoven term over which the parties negotiated. Should the courts create an interwoven exception for this tortious conduct as well? The answer is "no." There should be no exception for tortious conduct in either situation.

G. Punitive Damages

The narrow fraud in the inducement exception has a devastating impact on the award of punitive damages in a number of significant ways. First, it defeats two of the primary purposes of punitive damages. Second, the narrow exception creates a judicial exception to the Wisconsin statute authorizing punitive damages where none exists. Third, the narrow exception opens the door to reprehensible conduct that in the recent past has been appropriately redressed by Wisconsin courts.

Pursuant to Wisconsin statutes, punitive damages may be awarded where one party has acted in intentional disregard of the rights of the other party.¹⁶⁹ "A person acts in an intentional disregard of the rights of [another] if the person acts with the purpose to disregard the [other's] rights, or is aware that his or her acts are substantially certain to result in the plaintiff's rights being disregarded."¹⁷⁰ For a court to find an intentional disregard of the rights of the other party, the actor's conduct must be: (1) deliberate; (2) an actual disregard of the other's property right; and (3) sufficiently aggravated to warrant punishment.¹⁷¹ "The purpose of punitive damages is to punish . . . or deter the wrongdoer and others from engaging in similar conduct in the future."¹⁷² The amount of punitive damages awarded is such a sum as will accomplish the dual

169. WIS. STAT. § 895.043(3) (2005–2006).

170. Wis. JI–Civil 1707.1 (2007) (punitive damages: non-product liability).

171. *Id.*

172. *Id.*

purposes of punishment and deterrence.¹⁷³ Significantly, the deterrence purpose is to deter the current tortfeasor and others from committing the offending conduct. Punitive damages are rarely available in a breach of contract action. In fact, punitive damages are only available in a contract action when "the breach is also a tort for which punitive damages are recoverable."¹⁷⁴ In other words, despite the fact that a breach of contract has occurred, when there is an independent tort, punitive damages are available. This is the so-called tort exception to the contract rule.¹⁷⁵

Intentional misrepresentation via fraudulent inducement is an intentional tort that satisfies the tort exception permitting punitive damages, albeit there is also a breach of contract. Historically, both the breach of contract and independent tort were recognized and appropriate damages assessed. A party's intentional misrepresentation that induces the making of a contract gives the aggrieved party the power to avoid the contract.¹⁷⁶ It also gives the aggrieved party a claim for damages in tort.¹⁷⁷ The narrow exception to the economic loss doctrine, however, fundamentally changes this principle. The narrow exception provides that if the intentional misrepresentation relates to a matter that is interwoven with the contract, no independent cause of action in tort is available.¹⁷⁸ Without the independent tort, no punitive damages can be awarded.

Further, the adoption of the narrow exception reverses many years of well-established and sound Wisconsin jurisprudence regarding fraudulent inducement. For example, in *Lundin v. Shimanski*,¹⁷⁹ the seller of a rental property¹⁸⁰ fraudulently induced the buyer to enter into a purchase contract by falsely representing that the property was capable of being rented for income production and that the basement

173. *Id.*

174. RESTATEMENT (SECOND) OF CONTRACTS § 355 (1981).

175. *Id.* § 355 cmt b.

176. *Id.* § 164.

177. RESTATEMENT (SECOND) OF TORTS § 525 (1977).

178. *Kaloti Enters., Inc. v. Kellogg Sales Co.*, 2005 WI 111, ¶ 42, 283 Wis. 2d 555, ¶ 42, 699 N.W.2d 205, ¶ 42.

179. 124 Wis. 2d 175, 368 N.W.2d 676 (1985).

180. A rental property likely qualifies as a "product" since the construction of a home, *Linden v. Cascade Stone Co.*, 2005 WI 113, ¶ 25, 283 Wis. 2d 606, ¶ 25, 699 N.W.2d 189, ¶ 25, and a 42-unit condominium complex, *1325 N. Van Buren, LLC v. T-3 Group, Ltd.*, 2006 WI 94, ¶ 67, 293 Wis. 2d 410, ¶ 67, 716 N.W.2d 822, ¶ 67, are "products" under the economic loss doctrine.

was capable of being occupied.¹⁸¹ The Wisconsin Supreme Court had no difficulty in finding the seller's conduct evidenced a reckless disregard for the buyer's rights, and it affirmed an award of punitive damages against the seller. Significantly, the court noted:

Punitive damages are awarded to punish wrongdoing. To hold that punitive damages are improper in this case would shield the defendants from any liability beyond the costs of compensating the [plaintiffs] for their costs in putting the house in the condition it was represented to be in originally. But "putting the cookies back in the jar" when caught is not enough. If that result were reached, sellers could make any misrepresentation necessary to make a sale. If it was not discovered, or was discovered but not pursued, the seller would make a windfall gain. If the fraud were discovered and successfully proven, the seller would only be liable to make good on his representations. He would suffer no punishment nor would he be deterred from similar conduct in the future.¹⁸²

The fraudulent inducement in *Lundin* related to matters that were clearly interwoven as that term is described in the narrow exception. Thus, the fraud in the *Lundin* case would not be punished or deterred under the narrow exception. The narrow exception creates the very situation that the Supreme Court intended to avoid.

In *Jeffers v. Nysse*,¹⁸³ the seller fraudulently induced the buyers to enter into a purchase contract by knowingly misrepresenting the insulation and heating costs for a home¹⁸⁴ to be constructed by the sellers. The Wisconsin Supreme Court reasoned that when a party's motive of self-interest rises to the level of disregarding the rights of another, punitive damages are awarded to punish the wrongdoing.¹⁸⁵ Significantly, the court noted that to not allow punitive damages in a case like *Jeffers* "would shield the defendants from any liability beyond the costs of compensating the [buyers] for their costs in putting the

181. *Lundin*, 124 Wis. 2d at 178–81, 368 N.W.2d at 678–79.

182. *Id.* at 198–99, 368 N.W.2d at 687 (quoting *Jeffers v. Nysse*, 98 Wis. 2d 543, 553, 297 N.W.2d 495, 499 (1980)).

183. 98 Wis. 2d at 544–46, 297 N.W.2d at 495–96.

184. A contract for the construction of a new home is a "product" under the economic loss doctrine. *Linden*, 2005 WI 113, ¶ 25, 283 Wis. 2d 606, ¶ 25, 699 N.W.2d 189, ¶ 25.

185. *Jeffers*, 98 Wis. 2d at 551, 297 N.W.2d at 498–99.

house in the condition it was represented to be in originally.”¹⁸⁶ The court indicated that such a remedy would be an insufficient remedy and affirmed the punitive damage award. The court could find no logical basis for applying a different punitive damage standard in a case of fraudulent inducement to enter into a contract than that applied in other intentional tort actions.¹⁸⁷ The fraud in *Jeffers* clearly related to matters interwoven to the contract, and thus the independent tort would not be recognized under the narrow exception. Requiring the buyer to anticipate fraud and to assume, allocate, or insure against it, is focusing on the wrong party to the contract, and it is certainly not a sufficient basis for applying a different punitive damage standard for cases of fraudulent inducement than that applied in other cases of intentional torts.

In *Winkelman v. Kraft Foods, Inc.*,¹⁸⁸ a milk farmer entered into a contract to sell the farmer’s entire output of milk¹⁸⁹ to Kraft Foods. The case was tried before an arbitrator applying Wisconsin law. The arbitrator found that Kraft’s agent intentionally misrepresented to the farmers that they could get out of the contract at any time by paying one month’s penalty. The farmers indicated that Kraft’s agent “lied to get us to sign.”¹⁹⁰ The arbitrator determined that Kraft intentionally disregarded the farmers’ rights and awarded punitive damages against Kraft. On appeal, the court of appeals upheld the arbitrator’s award of punitive damages.¹⁹¹ Unquestionably, the fraudulent inducement concerned the farmers’ ability to terminate the contract, which is a term that would be interwoven under the narrow exception. Thus, the intentional tort would not be actionable, and no punitive damages would be awarded for the agent’s lies.

In *Rowell v. Ash*,¹⁹² the seller of a mobile home park¹⁹³ concealed defects in the park’s septic and well system. The trial court refused to

186. *Id.* at 553, 297 N.W.2d at 499.

187. *Id.* at 551, 297 N.W.2d at 499.

188. 2005 WI App 25, ¶ 2, 279 Wis. 2d 335, ¶ 2, 693 N.W.2d 756, ¶ 2.

189. This is an output contract under Wisconsin Statutes section 402.306, and the transaction is covered by the U.C.C.

190. *Winkelman*, 2005 WI App 25, ¶ 3, 279 Wis. 2d 335, ¶ 3, 693 N.W.2d 756, ¶ 3.

191. *Id.* ¶ 1, 279 Wis. 2d 335, ¶ 1, 693 N.W.2d 756, ¶ 1.

192. No. 98-2904-FT, 1999 WL 326205 (Wis. Ct. App. May 25, 1999).

193. A mobile home park likely qualifies as a “product” since the construction of a home, *Linden v. Cascade Stone Co.*, 2005 WI 113, ¶ 25, 283 Wis. 2d 606, ¶ 25, 699 N.W.2d 189, ¶ 25, and a 42-unit condominium complex, *1325 N. Van Buren, LLC v. T-3 Group, Ltd.*, 2006 WI 94, ¶ 67, 293 Wis. 2d 410, ¶ 67, 716 N.W.2d 822, ¶ 67, are “products” under the economic loss doctrine.

submit the buyers' claim for punitive damages to the jury.¹⁹⁴ On appeal, the court of appeals held that the buyers were entitled to a new trial on the issue of punitive damages. The appeals court noted that a jury question was fairly presented whether the sellers intentionally disregarded the buyers' rights.¹⁹⁵ The buyers asserted that the concealment of the defective well and septic system induced the sales contract and thereby disregarded their rights.¹⁹⁶ The state of the mobile home park's well and septic system was clearly interwoven with the sale of the park. Thus, under the narrow exception only the breach of contract action is available, and no jury question is presented for punitive damages.

In *Sassara v. Braun*,¹⁹⁷ a buyer purchased a plane¹⁹⁸ upon the seller's "representations that the plane had an airworthiness certificate and a fresh annual inspection." Both representations were knowingly false. The buyer brought an action to rescind the contract because of the intentional misrepresentation and also sought punitive damages. The court noted that although punitive damages are not available in a breach of contract action, they are available if the defendant has committed a tort and a breach of contract.¹⁹⁹ The court characterized the buyer's case as a fraud case seeking the remedy of rescission. In the court's opinion, this was not a straight breach of contract case. The court of appeals affirmed the lower court's damage award, which rescinded the contract; returned the purchase price, plus prejudgment interest; awarded incidental expenses; and awarded punitive damages for the seller's fraudulent inducement.²⁰⁰ Under the narrow exception to the economic loss doctrine, no tort would be recognized for the seller's lies regarding the plane's airworthiness and current annual inspection. Both items are interwoven with the contract, and thus no independent tort is available.²⁰¹

194. *Rowell*, 1999 WL 326205, at *2.

195. *Id.* at *6.

196. *Id.* at *1-2. See *Ollerman v. O'Rourke Co.*, 94 Wis. 2d 17, 30-31, 288 N.W.2d 95, 102 (1980); *Kaloti Enters., Inc. v. Kellogg Sales Co.*, 2005 WI 111, ¶ 13, 283 Wis. 2d 555, ¶ 13, 699 N.W.2d 205, ¶ 13 (finding that failing to satisfy a duty to disclose serves as a basis for a fraudulent inducement to contract claim).

197. No. 95-3300, 1997 WL 164020, at *2 (Wis. Ct. App. Apr. 9, 1997).

198. A U.C.C. transaction and clearly the sale of a "product" under the economic loss doctrine.

199. *Sassara*, 1997 WL 164020, at *5.

200. *Id.* at *1-2.

201. One could argue the "public safety" exception to the economic loss doctrine, but that exception has not been expanded beyond the use of asbestos in a shopping center. See

The narrow exception, by limiting a defrauded party to solely its contract remedy, provides little disincentive to an unscrupulous party. In *Radford v. J.J.B. Enterprises, Ltd.*,²⁰² two buyers purchased a boat²⁰³ that subsequently leaked due to dry rot in the boat's hull. The jury found that the seller intentionally misrepresented the soundness of the boat's hull prior to the sale.²⁰⁴ The seller represented to the buyers that all the dry rot was removed from the hull, and it was sound and seaworthy. The court noted that "[i]t [was] hard to imagine a representation more important to a prospective boat owner than soundness of the boat's hull."²⁰⁵ The seller's statements about the boat's hull concerned the fundamental element that makes a boat a boat. The jury found that the sellers fraudulently induced the buyers to purchase the boat and awarded compensatory and punitive damages. The court of appeals confirmed the damage awards.²⁰⁶ Under the narrow exception to the economic loss doctrine, the soundness of the hull would certainly be a matter interwoven with the contract.²⁰⁷ As such, the tort is not actionable, and no punitive damages would be available to deter this boat seller or others from lying in the future.

In *Smith v. Adcock*,²⁰⁸ a buyer was induced to purchase a 50% interest in a horse²⁰⁹ by fraudulent misrepresentations by the seller. The misrepresentations concerned the timing and terms of reselling the horse. Upon a finding of fraudulent inducement, the jury assessed \$25,000 in punitive damages against the seller.²¹⁰ Under the narrow exception, the seller's fraud arguably related to matters interwoven with the contract, and thus it is not actionable in tort. No punitive damages would be assessed for the seller's fraud or to deter other sellers.

Northridge Co. v. W.R. Grace & Co., 162 Wis. 2d 918, 922, 937-38, 471 N.W.2d 179, 180, 186 (1991).

202. 163 Wis. 2d 534, 541, 472 N.W.2d 790, 793 (Ct. App. 1991).

203. A U.C.C. transaction and clearly a sale of a "product" under the economic loss doctrine.

204. *Radford*, 163 Wis. 2d at 539, 472 N.W.2d at 792.

205. *Id.* at 544, 472 N.W.2d at 794.

206. *Id.* at 548-59, 472 N.W.2d at 796.

207. One could argue the "public safety" exception to the economic loss doctrine, but that exception has not been expanded beyond the use of asbestos in a shopping center. See *Northridge Co.*, 162 Wis. 2d at 922, 937-38, 471 N.W.2d at 180, 186.

208. *Smith v. Adcock*, No. 87-0088, 1987 WL 29666, at *1, *3 (Wis. Ct. App. Oct. 14, 1987).

209. A U.C.C. transaction and clearly a sale of a "product" under the economic loss doctrine.

210. *Smith*, 1987 WL 29666, at *2.

Finally, in *Spore v. Woodley*,²¹¹ buyers purchased a resort²¹² from the sellers based on the sellers' representations regarding the resort's gross revenues. Subsequent to the sale, it was determined that the amount of gross revenues stated by the sellers was false. The buyers sought rescission for the intentional misrepresentation and punitive damages. The trial court granted rescission of the contract and awarded restitution of monies paid by the buyers; prejudgment interest on the monies paid; incidental damages; and punitive damages. On appeal, the court affirmed the award of punitive damages for the intentional misrepresentation committed by the sellers.²¹³ Fraudulently misrepresenting the amount of gross revenues was one of the essential terms relied upon by the buyer that induced the buyer to purchase the resort. It was clearly interwoven with the contract negotiations. Nevertheless, under the narrow exception, the tort is not actionable, and the buyer has only contract damages available. No punitive damages are available.

The simplest analysis of the impact of the narrow exception to the economic loss doctrine on the award of punitive damages reflects that it is not sound public policy for a number of reasons. First, the narrow exception defeats two of the primary purposes of punitive damages, which are to punish and deter a deceitful tortfeasor and to deter others from using deceit in contract negotiations. The narrow exception ignores the tort in cases of fraud that are interwoven with the contract's formation. Thus, no punitive damages are available. Second, Wisconsin statutes authorize punitive damages where one party intentionally disregards the rights of another. There is no statutory exception for intentionally interfering with another's rights where the tort is fraud that is interwoven with a contract's formation. The narrow exception is a judicially created exception to a legislative enactment that has no exceptions. In addition, in 1995, when the punitive damage statute was passed, the supreme court had already upheld the award of punitive damages in the preceding fraudulent inducement cases.²¹⁴ If the

211. No. 85-0874, 1986 WL 217380 (Wis. Ct. App. May 20, 1986).

212. A resort likely qualifies as a "product" since the construction of a home, *Linden v. Cascade Stone Co.*, 2005 WI 113, ¶ 25, 283 Wis. 2d 606, ¶ 25, 699 N.W.2d 189, ¶ 25, and the sale of a 42-unit condominium complex, *1325 N. Van Buren, LLC v. T-3 Group, Ltd.*, 2006 WI 94, ¶ 67, 293 Wis. 2d 410, ¶ 67, 716 N.W.2d 822, ¶ 67, are "products" under the economic loss doctrine.

213. *Spore*, 1986 WL 217380, at *2.

214. See *supra* notes 179-87 and accompanying text (discussing supreme court decisions on punitive damages).

legislature had intended to reverse those awards by creating an exception, it would have done so. It did not. The inference is clear that no exceptions to the punitive damage statute should exist.

Finally, many years of Wisconsin jurisprudence have recognized the tort when one fraudulently induced another to enter into a contract with lies and deceit. The conduct has always been punished by punitive damages. Unfortunately, the adoption of the narrow exception reverses many years of well-established and sound Wisconsin jurisprudence regarding fraudulent inducement.

H. The Duty of Honesty and Fair Dealing

Every contract imposes upon each party a duty of honesty²¹⁵ and fair dealing.²¹⁶ A tort approach rather than a contract approach most effectively promotes this public policy of honesty and fair dealing between contracting parties.

Oftentimes, a breach of a contract duty and tort duty will overlap. "Ordinarily, a breach of contract is not a tort, but a contract may create the state of things which furnishes the occasion of a tort."²¹⁷ For example, "[a]ccompanying every contract is a common-law duty to perform with care, skill, [and] reasonable expedience" the contractual duties.²¹⁸ A negligent failure to perform such duties is a tort as well as a breach of contract.²¹⁹ Under such circumstances, the aggrieved party has a cause of action in both contract and tort and can often choose between the two.²²⁰ The economic loss doctrine, however, provides that a tort cause of action is not available if the breach of duty has caused only economic loss. The societal interest in the duty to perform the contract duties is not significant enough to permit a tort cause of action that ignores the contract terms. The contract remedy is the only remedy available.

215. The actual duty stated is "good faith and fair dealing." RESTATEMENT (SECOND) OF CONTRACTS § 205 (1981). Honesty and good faith are interchangeable, thus the duty of honesty and fair dealing. *Id.* § 205 cmt. a.

216. Specifically, the Restatement provides this duty in the performance and enforcement of the contract, not at formation. *Id.* § 205 cmts. a, b. However, the Wisconsin Supreme Court has recognized this duty at formation in *Ollerman v. O'Rourke Co.*, 94 Wis. 2d 17, 50-51, 288 N.W.2d 95, 111 (1980), and *Kaloti Enterprises, Inc. v. Kellogg Sales Co.*, 2005 WI 111, ¶ 20, 283 Wis. 2d 555, ¶ 20, 699 N.W.2d 205, ¶ 20.

217. *Colton v. Foulkes*, 259 Wis. 142, 146, 47 N.W.2d 901, 903 (1951) (quoting 38 AM. JUR. Negligence § 20 (1941)).

218. *Id.*, 47 N.W.2d at 903 (quoting 38 AM. JUR. Negligence § 20 (1941)).

219. *Brooks v. Hayes*, 133 Wis. 2d 228, 235, 395 N.W.2d 167, 170 (1986).

220. *Id.* at 246, 395 N.W.2d at 174.

A more difficult problem arises, however, when a contracting party is fraudulently induced to enter into a contract. The contractual duties arising from the contract exist. The societal duty to perform the contractual duties with reasonable care also exists. But, with the fraudulent inducement, an additional societal duty is breached. Wisconsin has a deeply rooted history in requiring honesty and fair dealing between contracting parties.²²¹ The duty protects the public interest in “formulating business judgments without being misled by others—that is, the interest in not being cheated.”²²² The societal duty to promote honesty and fair dealing in contractual relations includes the duty not to lie and a duty to disclose material facts in certain circumstances.²²³ Thus, the issue becomes whether the economic loss doctrine should still apply in the face of a party’s fraudulent inducement.

The narrow exception adopted in *Kaloti* provides that contract law shall control the parties’ dispute, despite one party’s deceitful conduct, provided the fraud relates to matters interwoven with the contract. On the other hand, if the fraud relates to extraneous matters, then tort remedies are available. In most cases of fraud in the inducement, the fraud will relate to an interwoven matter.²²⁴ In such cases, the contract remedies are the only ones available, not tort remedies. Thus, the societal duty to promote honesty and fair dealing is ignored. There is no price paid by the tortfeasor for his or her deceit. There is no message sent to others similarly situated to deter them from perpetrating fraudulent conduct. The predatory practices can continue, and the tortfeasor’s greatest exposure is to pay damages for the difference between the product’s actual value and the value as fraudulently represented.²²⁵ There is no exposure to punitive damages to punish the tortfeasor for his or her repugnant conduct. There is no punitive damage message to deter others from committing such predatory practices. In fact, the societal concern is completely ignored by adopting the narrow exception unless the fraud is found to be extraneous.

The rationale supporting the narrow exception is that the aggrieved party should negotiate his or her protection in the contract. There are, however, shortcomings to that rationale. First, should parties in a

221. *Ollerman*, 94 Wis. 2d at 50–51, 288 N.W.2d at 111; *Kaloti Enters., Inc.*, 2005 WI 111, ¶ 47, 283 Wis. 2d 555, ¶ 47, 699 N.W.2d 205, ¶ 47.

222. *Ollerman*, 94 Wis. 2d at 30, 288 N.W.2d at 101.

223. See *Kaloti Enters., Inc.*, 2005 WI 111, ¶ 20, 283 Wis. 2d 555, ¶ 20, 699 N.W.2d 205, ¶ 20.

224. See discussion *supra* Part VI (identifying the rare cases of extraneous fraud).

225. *Lundin v. Shimanski*, 124 Wis. 2d 175, 195, 368 N.W.2d 676, 686 (1985).

contract negotiation expect honesty and fair dealing from the other party, or expect fraud? The better policy would be to expect and encourage honesty and fair dealing, not fraud. Second, even if one party anticipates all the protection available by contract and negotiates contract warranty protection from fraud, the only remedy available to the aggrieved party in the event of fraud is the breach of contract action. Is it likely that the parties' negotiations will include a contract clause that makes punitive damages available in the event one party commits fraud? I think not. Further, should the promotion of such an important public policy be left to private contracting parties, or is this a matter best left to tort law to promote the societal interest? It seems clear that the public policy to promote honesty and fair dealings is most effectively promoted by a tort approach rather than a contract approach. The Wisconsin Statutes and Department of Agriculture, Trade, and Consumer Protection ("DATCP") regulations that redress falsely induced contracts use the tort approach, not the contract approach.²²⁶ The legislative approach uses the threat of costs and punitive damages to deter falsely induced contracts and to promote honesty and fair dealing between contracting parties. There is no exception for any kind of fraudulently induced contract. The legislature has chosen the tort approach to effectuate the duty of honesty and fair dealing. The courts should use the same approach.

I. Tort Principles Summary

The narrow exception clearly conflicts with established tort principles. First, a number of torts may be completely eliminated by the narrow exception. Promissory fraud is a tort that occurs when a promisor has no intent to perform a contractual promise at the time of contracting. It has been recognized in Wisconsin for seventy years. The narrow exception eliminates the tort of promissory fraud because a tort claim cannot be asserted for interwoven fraud. Since promissory fraud is fraud that relates to the actual promises in the contract, it is, by definition, interwoven fraud, not extraneous fraud. Any tort action under the narrow exception for interwoven fraud can only be brought as a contract action. Thus, the tort of promissory fraud has been eliminated.

Also, fraud in the factum/execution occurs when one misrepresents the character or nature of a contract and procures another's signature to it. Fraud in the factum/execution has always been recognized as a

226. See *infra* Part IX.

breach of one's public duty and a tort. The fraud relates to the character or nature of the contract and, as such, is the epitome of an interwoven term. Thus, under the narrow exception the tort claim is barred.

Second, there are a number of torts that are actionable because the societal wrong committed is separate and independent from the contract or prospective contractual relations. The contract is simply the occasion for the tort. The narrow exception fails to recognize this principle. For example, fraudulently inducing one not to enter into a contract or to perform one's contract is actionable as a tort despite the contractual background. Similarly, duress and fraud are actionable torts that both procure the creation of a contract. The contract is the occasion for the tort. A contract is formed under both circumstances. But there are two independent wrongs committed in the contracting process. One is fraud, and the other is compulsion. Tort law treats them as equal wrongs and actionable as such. The narrow exception precludes the tort action for interwoven fraud and thereby fails to recognize the deceit as a wrong independent from the contract. This is a significant failure of the exception.

Third, the narrow exception provides disparate treatment to parallel tort situations. The intentional tort of conversion occurs when the bailee in a bailment contract exceeds the authorized level of use specified in the contract. The unauthorized use is a material breach of contract. The unauthorized use is also a conversion under tort law. Similar to the situation of fraudulent inducement, the fraudulent inducement is a material breach of contract and also an intentional tort. In the bailment situation, the tort is actionable despite the companion breach of contract action. Under the narrow exception, the fraudulent inducement is not actionable if the fraud relates to interwoven terms. These are parallel situations that are treated differently under the law. Surely the deceitful conduct is a greater societal wrong than exceeding the authorized use in the contract.

Fourth, the narrow exception seriously undercuts the availability, purpose, and power of punitive damages. The victims of deceitful conduct are granted the right by statute to pursue punitive damages upon satisfying the statute's requirements.²²⁷ The narrow exception, by barring tort actions for interwoven fraud, is a judicially created exception to the punitive damage statute, where no exceptions were authorized by the statute. Further, the narrow exception, by not

227. WIS. STAT. § 895.043 (2005–2006).

permitting a tort action for interwoven fraud, defeats two of the primary purposes for punitive damages. It fails to punish and deter the tortfeasor, and it fails to deter others from engaging in fraudulent conduct in the future. Finally, and perhaps most distressing, the narrow exception prevents the assessment of punitive damages in many cases of egregious deceit that have been justifiably punished for many years in Wisconsin courts. The litany of past fraudulent actors that will now be able to avoid the full consequences of their deceit under the narrow exception is simply unjust.

Fifth, Wisconsin's proud history, which requires honesty and fair dealing between contracting parties, is not promoted by the narrow exception. Societal duties are advanced through tort law, and private duties are advanced through contract law. The duty of honesty and fair dealing is a public duty that is important enough to require a tort approach, not a contract approach. The narrow exception's insistence on a contract approach is not sufficient to ensure maximum compliance with the public duty of honesty and fair dealing.

IX. THE STATUTORY AND REGULATORY APPROACH TO FRAUDULENT INDUCEMENT

A. *Statutory Fraudulent Inducement*

The narrow fraud in the inducement exception conflicts with Wisconsin's fraudulent inducement statute. In 1995, the legislature passed Wisconsin Statutes section 895.80, which provides that "[a]ny person who suffers damage or loss by reason of intentional conduct that occurs on or after November 1, 1995" and also is in violation of Wisconsin Statutes section 943.20²²⁸ has a statutory cause of action against the person who caused the damage or loss.²²⁹ One violates section 943.20 by obtaining "title to property of another person by intentionally deceiving the person with a false representation which is known to be false, made with intent to defraud, and which does defraud the person to whom it is made."²³⁰ A "[f]alse representation" includes a promise made with intent not to perform it if it is part of a false and fraudulent scheme."²³¹ The legislature has made a decision that any

228. Wisconsin Statutes chapter 943 is "crimes against property," and section 943.20 specifically covers theft.

229. WIS. STAT. § 895.446 (2005–2006) (action for property damage or loss caused by crime) (previously section 895.80).

230. *Id.* § 943.20(1)(d).

231. *Id.*

person who suffers a criminal fraud in the inducement has a statutory civil cause of action against the person who caused the damage or loss.²³² Significantly, the authorizing statute further provides that a successful plaintiff is authorized to recover actual damages, all costs of investigation and litigation, and exemplary damages of not more than three times the actual damages.²³³ Further, the legislature has defined those damages that are recoverable as "actual damages," which includes "the retail or replacement value of damaged, used, or lost property, whichever is the greater."²³⁴ The itemized damages are clearly economic loss damages.²³⁵ The legislature has also authorized exemplary damages, which are punitive damages.²³⁶ The punitive damages are available without any additional proof other than that a criminal fraud in the inducement has occurred.²³⁷ Finally, the legislature also authorized recovery for all the costs of any investigation and litigation, which includes the value of time spent on the matter.²³⁸ Obviously, the legislature has made a significant public policy decision that criminal fraud in the inducement authorizes a civil fraud in the inducement case.

The narrow exception to the economic loss doctrine is in direct conflict with this legislative enactment. The narrow exception provides that fraud in the inducement that relates to interwoven terms can only be brought under contract law. The narrow exception clearly precludes a statutorily authorized civil cause of action for criminal fraud in the inducement. As such, the narrow exception is in conflict with the authorizing statute.²³⁹

There is only one decision addressing the conflict between the narrow exception and the authorizing statute. In *Below v. Norton*,²⁴⁰ buyers purchased a home after the sellers disclosed that the only plumbing defect was a defective bathtub drain handle. Subsequently, it was "discovered that the sewer line between the house and the street

232. *Id.* § 895.446(1). There are actually seventeen separate criminal statutory sections that, if violated, also give rise to a civil cause of action. *Id.*

233. *Id.* § 895.446(3).

234. *Id.* § 895.446(3)(a).

235. *See supra* Part V (defining economic loss damages).

236. WIS. STAT. § 895.446(3)(c).

237. *Id.*

238. *Id.* § 895.446 (3)(b).

239. *See id.* § 895.446.

240. No. 2005AP2855, 2006 Wisc. App. LEXIS 1092 (Nov. 21, 2006) (awaiting publication).

was broken.”²⁴¹ In their suit, the buyers alleged a statutory fraud in the inducement action. The court of appeals applied the narrow exception adopted in *Kaloti* and reasoned that the fraud in the inducement was not a matter “unrelated” to the contract.²⁴² As such, the economic loss doctrine barred the statutorily authorized fraud in the inducement action.²⁴³ This approach by the courts is in direct contravention to the legislature’s public policy decision.

“[D]etermination of public policy is a matter primarily for the legislature, and where the legislature has clearly stated its policy in the form of a statute, . . . that determination is binding on . . . the courts.”²⁴⁴ “[I]t is the duty of [the] court to apply the policy the legislature has codified in the statutes, not [to] impose [its] own policy choices.”²⁴⁵ Otherwise, the courts act as a super-legislature. The enactment of the criminal fraud in the inducement statute is a public policy statement that fraud in the inducement is a serious matter of public concern. In fact, it can rise to the level of criminal activity. The commission of criminal fraud in the inducement begets a statutory civil fraud in the inducement cause of action. Whether the fraud was extraneous or interwoven with the contract is not part of the analysis. The narrow exception clearly conflicts with the statutory authorization and cannot stand.

B. Wisconsin’s Deceptive Trade Practices Act

The narrow fraud in the inducement exception to the economic loss doctrine is completely eclipsed by the Wisconsin Deceptive Trade Practices Act (“DTPA”). Chapter 100 of the Wisconsin Statutes regulates marketing and trade practices. It is commonly referred to as the Deceptive Trade Practices Act. A significant part of the statute deals directly with sellers fraudulently inducing contracts for various products and services. The DTPA applies to consumer and commercial transactions. Obviously, the sale of products that result in economic loss to the buyer would be subject to the economic loss doctrine. The sale of services,²⁴⁶ of course, would not be subject to the doctrine.²⁴⁷ The DTPA

241. *Id.*

242. *Id.*

243. *Id.*

244. *Sinclair v. Dep’t Health & Soc. Servs.*, 77 Wis. 2d 322, 335, 253 N.W.2d 245, 251 (1977).

245. *Columbus Park Hous. Corp. v. City of Kenosha*, 2003 WI 143, ¶ 34, 267 Wis. 2d 59, ¶ 34, 671 N.W.2d 633, ¶ 34.

246. *See, e.g.*, WIS. STAT. § 100.177 (2005–2006) (noting that a fitness center is a business whose primary purpose is to provide services).

prohibits and sanctions sellers that fraudulently induce sales of particular products. For example, no person may make untrue, deceptive, or misleading representations to induce a contract for the sale of drugs,²⁴⁸ the sale of food,²⁴⁹ the sale of a vehicle product warranty,²⁵⁰ or the sale of a vehicle rust-proofing warranty.²⁵¹ For those fraudulently induced sales not covered by a specific statutory section, there is one section that provides very broad coverage. *No person may make "untrue, deceptive or misleading" representations to induce a contract for the "purchase, sale, hire, use or lease of any real estate, merchandise, securities, employment or services," or anything else.*²⁵² In addition to the express statutory prohibitions against fraudulently inducing contracts, there are companion provisions prohibiting deceptive advertising that may lead to the formation of a contract.²⁵³ The statute further provides that a person suffering pecuniary loss because of any statutory violation may sue in any court of competent jurisdiction and recover his or her pecuniary loss, together with costs and reasonable attorney's fees.²⁵⁴ This is a statutory remedy that supplements any other remedies an aggrieved person possesses.²⁵⁵ The purpose of all the statutory prohibitions against fraudulently inducing one into a contract is to protect the public from untrue, deceptive, or misleading representations.²⁵⁶ The DTPA is a clear statement of public policy sanctioning sellers who fraudulently induce contracts.

The narrow exception to the economic loss doctrine provides that a fraudulent inducement that relates to the terms and conditions of the contract is actionable only for breach of contract. That principle directly contradicts the DTPA mandate, which provides an independent cause of action for any fraudulent inducement that falls within the scope of the statute. The courts that have addressed the relationship between the economic loss doctrine and the DTPA's statutory prohibition and remedy have reached conflicting results. Some courts have concluded

247. *Ins. Co. of N. Am. v. Cease Elec. Inc.*, 2004 WI 139, ¶ 52, 276 Wis. 2d 361, ¶ 52, 688 N.W.2d 462, ¶ 52.

248. WIS. STAT. § 100.182(2) (2005–2006).

249. *Id.* § 100.183(1).

250. *Id.* § 100.203.

251. *Id.* § 100.205(5)(a).

252. *Id.* § 100.18(1).

253. *Id.* § 100.18(2), (3), (3m), (9)(a), and (10m).

254. *Id.* § 100.18(11)(b)2.

255. See *Kailin v. Armstrong*, 2002 WI App 70, ¶¶ 40–42, 252 Wis. 2d 676, ¶¶ 40–42, 643 N.W.2d 132 ¶¶ 40–42.

256. *Grube v. Daun*, 173 Wis. 2d 30, 57, 496 N.W.2d 106, 116 (1992).

that where the economic loss doctrine bars claims of common law fraudulent inducement (interwoven fraud), the economic loss doctrine also bars claims under the DTPA.²⁵⁷ Others have concluded that the economic loss doctrine should not bar fraudulent inducement claims under the DTPA.²⁵⁸ The Wisconsin Supreme Court has not yet decided the issue, although in dictum it suggested that the economic loss doctrine may not be a bar to a claim under the DTPA.²⁵⁹

The weight of case authority clearly indicates that the economic loss doctrine should not be a bar to any fraudulent inducement actions under the DTPA whether the fraudulent inducement relates to interwoven or extraneous matters. The weight of authority is correct. “[D]etermination of public policy is a matter primarily for the legislature, and where the legislature has clearly stated its policy in the form of a statute, . . . that determination is binding on . . . the courts.”²⁶⁰ If the supreme court and the legislature differ on public policy, the legislature’s view must control.²⁶¹ The supreme court’s *Kaloti* decision, adopting the principle that contracts induced by fraud on interwoven terms can be brought only in contract, directly conflicts with the statutory mandate of the DTPA and its companion sections. The DTPA sections supersede the narrow exception, not vice versa. Thus, an aggrieved party that is fraudulently induced to purchase a “product” can sue under Wisconsin Statutes section 100.18 to recover his or her pecuniary loss and attorneys fees despite the fact that the fraud may be interwoven.

In addition, punitive damages are also available as part of a claim asserted under the DTPA if the prerequisites for punitive damages are

257. *MBI Acquisition Partners, L.P. v. Chronicle Publ’g Co.*, 301 F. Supp. 2d 873, 886 (W.D. Wis. 2002); *Weather Shield Mfg., Inc. v. PPG Indus.*, No. 97-C-707-S, 1998 U.S. Dist. LEXIS 22489, at *11–*15 (W.D. Wis. June 10, 1998).

258. *Dow v. Poltzer*, 364 F. Supp. 2d 931, 938–39 (E.D. Wis. 2005); *Seibel v. A.O. Smith Corp.*, No. 97-C-0874-S, 1998 U.S. Dist. LEXIS 19903, at *7, *10 (W.D. Wis. Apr. 2, 1998); *Stoughton Trailers, Inc. v. Henkel Corp.*, 965 F. Supp. 1227 (W.D. Wis. 1997); *Peterson v. Cornerstone Prop. Dev., LLC*, 2006 WI App 132, ¶ 30, 299 Wis. 2d 800, ¶ 30, 720 N.W.2d 716, ¶ 30; *Carlson v. Gleichsner*, No. 04-1376, 2005 WL 241168, at *5 (Wis. Ct. App. Feb. 3, 2005); *Kailin*, 2002 WI App 70, ¶¶ 42–43, 252 Wis. 2d 676, ¶¶ 42–43, 643 N.W.2d 132, ¶¶ 42–43.

259. *Van Lare v. Vogt, Inc.*, 2004 WI 110, ¶ 23, 274 Wis. 2d 631, ¶ 23, 683 N.W.2d 46, ¶ 23.

260. *Sinclair v. Dep’t of Health & Soc. Servs.*, 77 Wis. 2d 322, 335, 253 N.W.2d 245, 251 (1977).

261. *Columbus Park Hous. Corp. v. City of Kenosha*, 2003 WI 143, ¶ 34, 267 Wis. 2d 59, ¶ 34, 671 N.W.2d 633, ¶ 34.

satisfied.²⁶² Wisconsin law requires a showing that the defendant either acted maliciously or in intentional disregard of the rights of the injured party.²⁶³ Thus, the DTPA statutory claim is tantamount to a tort claim, not a contract claim.

The elements for a common law fraud in the inducement claim in Wisconsin are: (1) the defendant makes a factual representation; (2) the representation is untrue; (3) the defendant knowingly or recklessly made the untrue representation; (4) the representation is made with the intent to defraud; (5) the aggrieved party reasonably relies on the representation; and (6) the representation occurred before the contract was formed.²⁶⁴ The elements of a statutory claim for fraudulent inducement under the DTPA require that (1) the representation occurs before the contract is formed; (2) the representation must be untrue, deceptive, or misleading; and (3) the representation must be to the public.²⁶⁵ Some courts have also suggested that the aggrieved party must reasonably rely on the representation as well.²⁶⁶

A simple comparison suggests that the two differences between the DTPA statutory claim of fraudulent inducement and a common law claim are the requirements of the intent element in the common law claim and the representation to the "public" in the statutory claim. Case law decided under the DTPA is clear that a representation between two contracting parties prior to contracting satisfies the statutory public requirement.²⁶⁷ Thus, no difference exists between the statutory and common law claims on the statutory public requirement. The only significant difference between the two claims is that the common law

262. *Radford v. J.J.B. Enters., Ltd.*, 163 Wis. 2d 534, 548–49, 472 N.W.2d 790, 796 (Ct. App. 1991); *Hines v. Camosy*, No. 88-2247, 1989 WL 142779, at *1 (Wis. Ct. App. Sept. 20, 1989).

263. WIS. STAT. § 895.043(3) (2005–2006).

264. *See Kaloti Enters., Inc. v. Kellogg Sales Co.*, 2005 WI 111, ¶ 12, 283 Wis. 2d 555, ¶ 12, 699 N.W.2d 205, ¶ 12.

265. WIS. STAT. §100.18 (2005–2006) (fraudulent representations).

266. *Novell v. Migliaccio*, No. 2005AP2852, 2006 WL 2947041, at *3, (Wis. Ct. App. Oct. 17, 2006); *Below v. Norton*, No. 2005AP2855, 2006 Wisc. App. LEXIS 1092, at *8 (Nov. 21, 2006).

267. *State v. Automatic Merchandisers of Am., Inc.*, 64 Wis. 2d 659, 663–65, 221 N.W.2d 683, 686 (1974); *Kailin v. Armstrong*, 2002 WI App 70, ¶ 44, 252 Wis. 2d 676, ¶ 44, 643 N.W.2d 132, ¶ 44; *K&S Tool & Die Corp. v. Perfection Mach. Sales, Inc.*, 2006 WI App 148, ¶ 23, 720 N.W.2d 507, ¶ 23. *But see D & B Auto. Equip., Inc. v. Snap-On, Inc.*, No. 03-CV-141, 2006 U.S. Dist. LEXIS 17329, at *17, *21 (E.D. Wis. Mar. 27, 2006); *Donisi v. McGann*, No. 2005API748-FT, 2005 WL 3116170, at *13 (Wis. Ct. App. Nov. 23, 2005); *Mayville Die & Tool, Inc. v. Weller Mach. Co.*, No. 01-1509-FT, 2001 WL 1512917, ¶ 3 (Wis. Ct. App. Nov. 29, 2001).

claim has an intent element that must be satisfied. The statutory claim does not require proof of any intent to make a false representation, and thus is intent-neutral.²⁶⁸ Since all of the elements for the statutory and common law claims of fraudulent inducement are the same, with only the one exception, the statutory claim will be easier to prove than the common law claim. Further, the statutory claim covers contracts that relate to real estate, merchandise, securities, employment, service, or “anything offered to the public for sale, hire, use, or lease.”²⁶⁹ The scope of the statutory claim of fraudulent inducement is much broader than the narrower scope of the economic loss doctrine which applies only to contracts for “products.” Thus, one can fairly conclude that the DTPA statutory claim for fraudulent inducement renders the economic loss doctrine, and its appendant issue of whether the fraud is interwoven or extraneous, a moot question. In sum, the DTPA renders the narrow exception meaningless as a matter of implicit preemption by the DTPA’s statutory authorization or moot because of the broader scope of the DTPA.

C. The Department of Agriculture, Trade, and Consumer Protection Regulations

The narrow fraud in the inducement exception to the economic loss doctrine conflicts with the regulations promulgated by the DATCP and its authorizing statutes. The Wisconsin legislature granted the DATCP the authority to promulgate regulations to implement chapters 93-100 of the Wisconsin Statutes.²⁷⁰ The regulations promulgated by the DATCP have the force of law.²⁷¹ In addition, section 100.20 of the Wisconsin Statutes grants the DATCP the authority to promulgate regulations that forbid unfair methods of competition or trade practices.²⁷² The DATCP has promulgated a series of rules that have a diverse scope. In large part, the regulations specify and prohibit a number of unfair trade practices that fraudulently induce contracts. The specific statutory areas prohibiting fraudulently induced contracts are: home improvement practices;²⁷³ basement waterproofing practices;²⁷⁴ real estate

268. *Stuart v. Weisflog’s Showroom Gallery, Inc.*, 2006 WI App 184, ¶ 28, 722 N.W.2d 766, ¶ 28.

269. WIS. STAT. § 100.18(1) (2005–2006) (emphasis added).

270. *Id.* § 93.07(1) (department duties).

271. *Id.*

272. *Id.* § 100.20(2) (methods of competition and trade practices).

273. WIS. ADMIN. CODE ATCP § 110.02 (2004).

274. WIS. ADMIN. CODE ATCP § 111.03 (2006).

advertising;²⁷⁵ art prints and multiple art sales practices;²⁷⁶ chain distribution schemes;²⁷⁷ telecommunications and cable television services;²⁷⁸ mobile home parks;²⁷⁹ direct marketing;²⁸⁰ coupon sales promotions;²⁸¹ and motor vehicle repair.²⁸² Some of the prohibitions apply to only consumer contracts,²⁸³ and others have application to commercial and consumer contracts.²⁸⁴

The DATCP regulation with the broadest application to the economic loss doctrine is DATCP section 127, which regulates direct marketing. The direct marketing regulation applies to consumer transactions in goods and services.²⁸⁵ DATCP section 127 provides that no seller may “[m]isrepresent the nature, quantity, material characteristics, performance or efficacy of the goods or services offered or promoted by a seller.”²⁸⁶ Unquestionably, the direct marketing regulations apply to the sale of a product, and upon the occurrence of an economic loss, the economic loss doctrine will apply. More particularly, if the sale is fraudulently induced, the narrow exception provides that for interwoven terms, the aggrieved party’s remedy is solely breach of contract. The regulations provide that a violation occurs if a seller “[m]isrepresent[s] the nature, quantity, material characteristics, performance or efficacy of the goods.”²⁸⁷ Clearly, the regulations prohibit a seller from fraudulently inducing a contract by misrepresenting any terms, including interwoven terms.

The authorizing statute also provides that any violation of the DATCP’s regulations permits the aggrieved party to sue for damages and recover twice the amount of the pecuniary loss, together with costs and attorney’s fee.²⁸⁸ There are a number of purposes served by the statutory remedies. “First, the recovery of double damages and attorney

275. WIS. ADMIN. CODE ATCP § 114.02 (2004).

276. *Id.* § 117.10.

277. *Id.* § 122.01.

278. *Id.* § 123.10.

279. *Id.* § 125.09.

280. WIS. ADMIN. CODE ATCP §§ 127.14, 127.44, 127.72 (2006).

281. WIS. ADMIN. CODE ATCP § 131.07 (2006).

282. WIS. ADMIN. CODE ATCP § 132.09 (2004).

283. WIS. ADMIN. CODE ATCP §§ 110.01(1), 111.01, 123.01(13), 125.01(1), 127.01(2) (2006).

284. *Id.* chs. 114, 117, 122, 131, 132.

285. *Id.* §§ 127.14(5), 127.44(5), 127.72(5).

286. *Id.* § 127.14(5).

287. *Id.*

288. WIS. STAT. § 100.20(5) (2005–2006).

fees encourages [aggrieved parties] to bring legal actions to enforce their rights under the administrative regulations.”²⁸⁹ Second, the aggrieved parties who sue act as “private attorney[s] general” who not only enforce their individual rights, but the aggregate of the individual suits enforces the public’s rights.²⁹⁰ Third, the aggrieved-party suits that subject violators to double damages have the effect of deterring unacceptable conduct. And finally, the private attorney general suits “provide a necessary backup to the state’s enforcement powers.”²⁹¹

A recent case illustrates the correct relationship between the DATCP regulations and the economic loss doctrine’s directive to limit an aggrieved party to his or her contract remedies. In *Stuart v. Weisflog’s Showroom Gallery, Inc.*,²⁹² homeowners were fraudulently induced to enter into an architectural and remodeling contract in violation of DATCP section 110. The homeowners sued and sought damages under section 100.20(5). The court concluded that the economic loss doctrine was not applicable because the contracts were primarily for services.²⁹³ Nevertheless, the court analyzed the relationship between the economic loss doctrine and the DATCP code violations. The court noted that the claims arising from the administrative code violations are tort-based, not contract-based. Further, the court reasoned that the statutory cause of action for fraudulent inducement is “separate and apart from any breach of contract” action.²⁹⁴ The court noted that there is no indication that the legislature, by passing the authorizing legislation, “intended to simply add a remedy to common law misrepresentation claims or breach of contract claims.”²⁹⁵ The court concluded by stating that to apply the economic loss doctrine to a proven DATCP violation would defeat the

289. *Shands v. Castrovinci*, 115 Wis. 2d 352, 358, 340 N.W.2d 506, 509 (1983).

290. *Id.* at 358, 340 N.W.2d at 509.

291. *Id.*

292. 2006 WI App 109, ¶ 17, 293 Wis. 2d 668, ¶ 17, 721 N.W.2d 127, ¶ 17; *see also* *Carlson v. Gleichsner*, No. 04-1376, 2005 WL 241168, at *5 (Wis. Ct. App. Feb. 3, 2005) (noting that the economic loss doctrine would not be a bar to a violation of Wisconsin Administrative Code of Transportation section 139.03(1)). Section 139.03 prohibits the use of false, deceptive, or misleading representation to induce the purchase of a motor vehicle. WIS. ADMIN. CODE TRANS. § 139.03(1) (2004).

293. *Stuart*, 2006 WI App 109, ¶ 28, 293 Wis. 2d 668, ¶ 28, 721 N.W.2d 127, ¶ 28; *see also* *Stuart v. Weisflog’s Showroom Gallery, Inc.*, 2006 WI App 184, 296 Wis. 2d 249, 722 N.W.2d 766.

294. *Stuart*, 2006 WI App 109, ¶ 26, 293 Wis. 2d 668, ¶ 26, 721 N.W.2d 127, ¶ 26.

295. *Id.* ¶ 33, 293 Wis. 2d 668, ¶ 33, 721 N.W.2d 127, ¶ 33.

public purpose underlying section 100.20.²⁹⁶ “[R]emedial statutes should be liberally construed to suppress the mischief and advance the remedy that the statute intended to afford.”²⁹⁷

In addition to authorizing a statutory cause of action for falsely inducing contracts in violation of DATCP regulations, the statute also authorizes double damages and the recovery of attorney’s fees.²⁹⁸ Courts have also permitted a plaintiff to elect punitive damages in lieu of the statutorily authorized double damages.²⁹⁹ Thus, an aggrieved party who has been falsely induced to enter into a contract in violation of the DATCP regulations has a statutory right to sue to recover his pecuniary loss, plus attorney’s fees, and if the circumstances merit, punitive damages. These rights are in direct derogation to the economic loss doctrine, which restricts an aggrieved party to only the contract remedy. Further, the narrow exception would only permit a tort cause of action if the false material related to an extraneous contact matter. No such restriction is imposed under the statutory cause of action for a violation of DATCP regulations. Thus, the statutory cause of action pursuant to the authorizing statute and DATCP regulations supersedes the economic loss doctrine and the narrow exception.

D. Statutory and Regulatory Summary

The narrow exception is in direct conflict with a number of Wisconsin statutes and regulations that were enacted to redress fraudulently induced contracts. An aggrieved party has a statutorily authorized civil cause of action against a tortfeasor who has criminally and fraudulently induced him or her to transfer his or her property to another. The statute authorizes the aggrieved party to recover any economic losses, costs, and punitive damages.³⁰⁰ The legislature’s approach is a tort approach to redress fraudulently induced contracts, not a contract approach. The focus is on the tortfeasor’s conduct, not the buyer’s contract negotiating acumen. No duty is placed on the buyer to assume, allocate, or ensure against the fraud in the contract. The narrow exception, which bars a tort action for interwoven fraud, directly conflicts with the statutorily authorized civil cause of action.

296. *Id.* ¶ 34, 293 Wis. 2d 668, ¶ 34, 721 N.W.2d 127, ¶ 34.

297. *Benkoski v. Flood*, 2001 WI App 84, ¶ 8, 242 Wis. 2d 652, ¶ 8, 626 N.W.2d 851, ¶ 8.

298. WIS. STAT. § 100.20(5) (2005–2006).

299. *See, e.g., Seay v. Gardner*, No. 94-1933-FT, 1995 WL 556273, at *2–*3 (Wis. Ct. App. Sept. 21, 1995); *Zablocki v. Hoefs*, 128 Wis. 2d 560, 384 N.W.2d 367 (Ct. App. 1986) (unpublished).

300. *See* WIS. STAT. § 895.446(3) (2005–2006).

The Wisconsin DTPA regulates marketing and trade practices. One particularly broad provision of the DTPA prohibits fraudulently inducing a contract for the purchase, sale, hire, use, or lease of any real estate, merchandise, securities, employment, service, or anything else.³⁰¹ Any violation of the DTPA creates a cause of action that permits a buyer to recover any economic loss, costs, attorney's fees, and punitive damages.³⁰² The DTPA approach to fraudulently induced contracts is a tort approach, not a contract approach. No duty is placed on the buyer to assume, allocate, or insure against fraud. The DTPA's focus is on the tortfeasor's misconduct, not the buyer's negotiating ability. The narrow exception, which bars any tort action for interwoven fraud, clearly conflicts with the DTPA. As such, the narrow exception is likely rendered moot as a matter of implicit preemption by the DTPA's broad coverage and statutorily authorized cause of action.

Finally, the Wisconsin DATCP has promulgated regulations that forbid various unfair trade practices, including fraudulently inducing a consumer to enter into a contract for goods and services. An aggrieved consumer is authorized by statute to sue for any violation of DATCP regulations.³⁰³ The aggrieved consumer is statutorily authorized to recover twice his pecuniary loss, costs, and attorney's fees. Punitive damages can also be elected in lieu of the double damages.³⁰⁴ The statutory approach for fraudulently inducing a consumer contract in violation of DATCP regulations is a tort approach, not a contract approach. No duty is placed on the buyer to assume, allocate, or insure against fraud. The DATCP regulations' focus is on the tortfeasor's misconduct, which is the source of the problem. Again, the narrow exception, which bars any tort action for interwoven fraud, clearly conflicts with the authorized tort remedy for fraudulently inducing contracts in violation of DATCP regulations.

X. CONCLUSION

The narrow fraud in the inducement exception to the economic loss doctrine is not a sound principle. It conflicts with established precedent under contract and tort law and conflicts with Wisconsin statutes and regulations. For example, established contract principles dealing with fraud under the parol evidence rule and as is clauses have always

301. *See id.* § 100.18(1).

302. *See id.* § 100.20(5).

303. *See id.*

304. *See supra* note 299 and accompanying text.

permitted a tort action for any type of fraud. Further, contract clauses that exculpate one for his or her intentional torts are against public policy and not enforceable. Similarly, the narrow exception's tort bar for interwoven fraud is against public policy. Tort principles are also adversely affected by the adoption of the narrow exception. The torts of promissory fraud and fraud in the factum/execution are eliminated by barring tort actions for interwoven fraud. Unlike other torts committed in the context of a contractual setting that are deemed independent torts separate and apart from the contract, interwoven fraud is not considered an independent tort. Under tort law, duress and fraud are considered to be the same specie of tort. They both wrongfully induce the formation of a contract. The narrow exception, however, treats them differently by creating a tort exception for interwoven fraud. The narrow exception also requires different treatment for virtually identical torts. A bailee who exceeds the authorized use for bailed property commits a breach of contract and the tort of conversion. The tort is actionable. One who commits fraud in the inducement commits a breach of contract and the tort of intentional misrepresentation. The tort is not actionable for interwoven fraud. Punitive damages cannot be assessed when interwoven fraud is involved because the sole remedy is contract law. The tortfeasor's deceitful conduct goes unpunished, and no message or the wrong message is sent to others who may be watching. Also, the public duty to be honest in contractual dealings is not promoted by the narrow exception, since only contract remedies are available for interwoven fraud. Finally, the narrow exception conflicts with the various statutory causes of action authorized by Wisconsin Statutes, including the Wisconsin DTPA, and it conflicts with DATCP regulations. The statutory and regulatory approach to redressing fraudulently induced contracts is a tort approach. Both focus on the tortfeasor, not the victim. The burden is placed on the tortfeasor and others similarly situated not to commit fraudulent conduct. For many reasons, the narrow fraud in the inducement exception is simply not the correct exception needed for fraud.

The broad exception is clearly the better exception. It correctly redresses all deceitful conduct and treats it as tortious behavior. The broad exception avoids all the conflicts with tort and contract law. Finally, the broad exception follows the tort approach as adopted by the Wisconsin statutes and regulations in redressing fraudulently induced contracts.